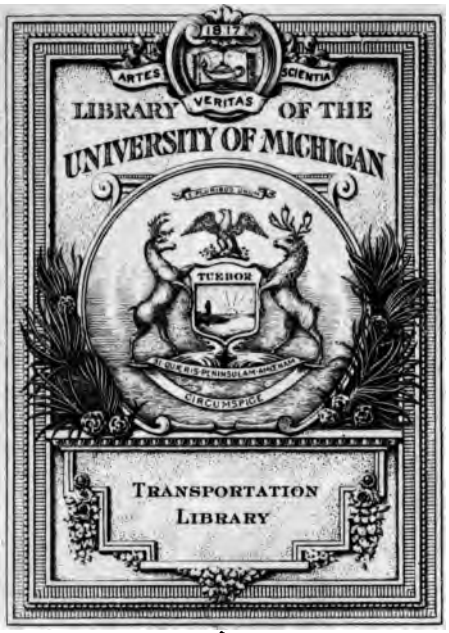

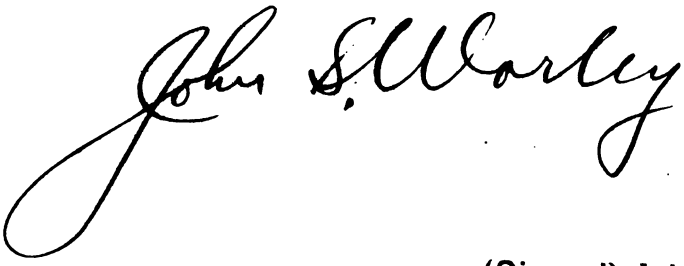

(Signed) John S. Worley

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AS
PUBLIC AGENTS

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A STUDY IN SOVEREIGNTY

BY

BROOKS ADAMS

WITH AN HISTORICAL FINANCIAL ANALYSIS OF THE GREAT NORTHERN RAILWAY SYSTEM

BY

FREDERICK O. DOWNES

BOSTON

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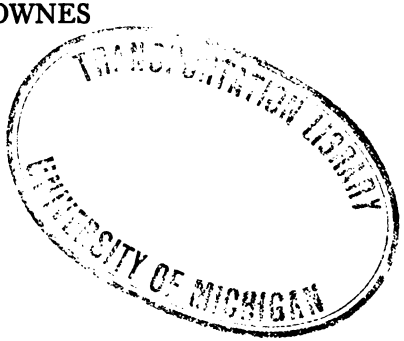

BOSTON

1910

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PREFACE

SPOKANE, in the State of Washington, lies on the western slope of the Rocky Mountains, roughly speaking about four hundred miles from the Pacific coast and ninety miles from the Canadian border. It is the converging point of all the transcontinental lines traversing the Northwest, and the natural capital of the country between the Rocky and the Cascade ranges. As Mr. Hill long ago pointed out, it is the gateway to this important region, and should be a great commercial and industrial centre. It has, however, suffered from discrimination in railway rates. When the first railways were built, land transportation from the Atlantic to the Pacific coast was more or less affected by water competition from Atlantic ports round the Horn. The rates to San Francisco, Portland, Seattle and other Pacific terminals were, therefore, adjusted according to a supposed relation to ocean freights. Interior points, such as Spokane, were, on the contrary, subject to an absolute railway monopoly, and the rates made to them were arbitrarily higher. In theory these rates were formed by combining the terminal rate to the Pacific coast with the local back to the interior point, on the principle that this price represented what it would cost the inhabitants of the interior town to ship their goods from New York round Cape Horn, and then forward them from the coast to their domicile. In practice the rates made to points under monopoly

were "all that the traffic would bear." In the case of Spokane they averaged an advance on the rates to Seattle, four hundred miles further from the initial point, approximately, in the ratio of $1.50 to $1.00 for identical service, in the same cars, over the same track, and in trains all of which stopped at Spokane before moving west from Spokane toward Seattle.

Spokane always resisted this system, and on April 2, 1889, an association of citizens called the Merchants' Union of Spokane Falls filed a petition, under the statute of 1887, regulating interstate commerce, praying that the Interstate Commerce Commission would equalize their rates with the rates to the coast. At the hearing evidence of water competition at the coast was introduced by the defendants, and the Commission found as a fact that such competition existed. The legal conclusion followed, under the decisions of the Commission, that "dissimilar conditions" prevailed as between Spokane and Seattle, thus justifying the roads in disregarding the fourth or the Long and Short Haul clause of Chapter 104 of the Acts of 1887, which forbade the greater charge for the lesser distance, where the conditions were "similar." Merchants' Union of Spokane Falls *v.* Northern Pacific R.R., 4 I. C. Rep., 183, following In re Louisville & Nashville R. R. Co., 1 I. C. Rep., 279; and Trammell *v.* Clyde S. S. Co. et al., 4 I. C. Rep., 120. These last two decisions were afterward affirmed and extended by the Supreme Court in the line of cases beginning with Interstate Commerce Commission *v.* Alabama Midland Ry. Co., 168 U. S., 144.

Conceding that the Long and Short Haul clause did not apply, the Commission then considered the reasonableness of the rates charged Spokane. It found them

unreasonable, and reduced them according to a schedule set forth in an order, 4 I. C. Rep., 197. The road declined to obey this order, and the Farmers' Loan and Trust Company, acting for the petitioners, brought process for enforcement. After trial in the Circuit Court of the United States the petition was dismissed on October 16, 1897, on the ground that the Supreme Court of the United States had held that the Interstate Commerce Commission had no power to fix rates. Farmers' Loan & Trust Co. *v.* Northern Pacific Ry. Co., 83 Fed. Rep., 249, citing Interstate Commerce Commission *v.* Cincinnati, N. O. & Texas Pacific Ry. Co., 167 U. S., 479.

This decision temporarily stopped the litigation, giving the railways absolute control of the situation, but in 1906 Congress amended the statute regulating interstate commerce. By Section 4 of Chapter 3591 of the Acts of 1906, Congress empowered the Interstate Commerce Commission to fix reasonable rates. On the day this law went into effect Spokane filed a second petition praying for relief against the three transcontinental lines which, at that time, converged there. Answers were filed by the Northern Pacific, the Great Northern, and the Union Pacific, and by order of the Commission a large number of connecting roads were served with process.

The first hearing was held at Spokane, and there delegations of citizens representing various organizations in Portland, San Francisco and elsewhere, appeared and obtained permission to file petitions as interveners in order to protect the interests of the cities on the Pacific coast, which they alleged were threatened by the demand for an equalization of rates made by Spokane. A mass of testimony was taken at Spokane, and subsequently

at other hearings held at Chicago and Portland, and the case was argued before the Commission in Washington on June 27 and 28, 1907. At Spokane the complainants introduced evidence tending to show excessive profits by the roads. In order to controvert this evidence the Great Northern and Northern Pacific examined experts at Chicago to prove the value of the properties. At Portland this valuation was criticised by Mr. H. P. Gillette, an engineer of the highest authority, who was then engaged in valuing the railways of the State of Washington for the State Government, and who was assigned without a fee, by the Railroad Commission of the State of Washington, for this service, on application made by the complainants. The extent to which such evidence of value was relevant in this cause was afterward argued at Washington. In view of the importance of the controversy the Commission, after the argument, propounded certain questions to counsel, and directed that supplementary briefs should be filed in three months. Finding that these questions could only be answered by an examination of the relation which railways as highways bear both to the United States and to the people, I prepared the following pamphlet with the help of Mr. Downes. I asked Mr. Downes to examine the official financial documents of the Great Northern system, expecting to show that an undue tax was being levied upon the public. The work as done by Mr. Downes has gone much further. I apprehend that his analysis demonstrates that the uncontrolled methods of monopolistic administration of railways, which have hitherto been tolerated in the United States, are incompatible with the continuance of constitutional government. The

presentation of both the law and the facts touching these questions is as complete as the time at our disposal permitted us to make it, and is reprinted substantially in its original form, one case only, accidentally omitted, having been inserted in the text of the argument, and a few pages added to the analysis.

On February 9, 1909, the Commission entered judgment, City of Spokane et al. *v.* Northern Pacific Ry. Co. et al., 15 I. C. C. Rep., 376. In the opinion, Prouty, C., considered, without deciding, the various legal propositions which I have advanced, but found as a fact that the Spokane rates were unreasonable, and entered an order directing reduction, to take effect May 1. The order, however, permitted the carriers to present some scheme of adjustment of their own before that date. This the carriers did. Spokane rejected the adjustment, and the litigation is still pending.

BROOKS ADAMS.

BOSTON, *March* 10, 1910.

RAILWAYS AS PUBLIC AGENTS

CITY OF SPOKANE ET AL.

v.

NORTHERN PACIFIC RAILWAY ET AL.

AFTER hearing argument in this cause in Washington, on June 27 and 28, 1907, the Interstate Commerce Commission directed counsel to prepare supplementary briefs upon sundry questions of law, but more particularly upon the legality of the method employed by the Great Northern and Northern Pacific railways in the valuation of their property.

These defendants, in order to show the reasonableness of the total revenue drawn by them from the public, valued the entire property employed by the corporations in the public service, and then deducting the cost of operation, taxes, and depreciation from their gross receipts, calculated the balance as a species of rental upon the sum total which their schedules showed.

In drawing up their schedules these defendants entered thereon all land to which they claimed title, however acquired, whether by private gift, government grant, condemnation proceedings under eminent domain, or amicable purchase, and whether the land bought was paid for

with money contributed by stockholders from their own funds, or with money appropriated to the purpose out of surplus earnings, after operating expenses, taxes, depreciation, fixed charges, and dividends had been defrayed. The entire acreage thus obtained the defendants caused their own officials to appraise at its supposed present market value, thus charging the "unearned increment" to capital, and it was upon this valuation that the rental the public owed the companies for the use of the land as a highway was calculated.

The chief questions propounded by the Commission for argument related to this method of valuing the defendants' land. The land itself naturally falls into four categories: 1st, Land acquired as a donation from private persons, in the expectation of receiving some consideration in the nature of improved service. 2d, Land used for railway purposes, such as right of way, which had been granted by government. 3d, Land acquired by the company either by exercise of the right of eminent domain, or by voluntary sale, but, however acquired, land which had been paid for with money appropriated from surplus income. 4th, Land acquired by the company in any manner, the cost of which had been defrayed with money drawn from the private means of stockholders.

The first question was, whether all these four categories of land could be entered upon the defendants' schedules as forming part of the total valuation of the corporate property on which the public should pay a return; and if all the categories could not be so entered, then which should be excluded. The second question was, whether the "unearned increment" upon any land whatever, however acquired, which increment had accrued since the acquisition of said land by the company, could be valued as part of the corporate capital on which the public should pay a return or rental.

I apprehend that the issues here presented go to the root not only of the relation of the railway corporation to the State, but of the relation of all American governments to the people. The reason is obvious. If an American government be a public trustee who cannot divest himself of his trust, and if the railway company be an agent of that trustee employed to build and administer a highway, for the sole reason that a particular form of highway can be better administered by a private agent than by the people in their corporate capacity, then a fiduciary relation is established between the corporation and the public whose limitations are sharply defined.

If, on the contrary, American governments are not public trustees, or can divest themselves of the sovereign functions which they hold in trust in favor of private persons who may exercise sovereign power thus granted without accountability, then the defendants will not only have established their contention in this cause, but they will have established their sovereignty over this nation, so far as sovereignty can be established by judicial decision.

The first point to determine is what constitutes sovereignty. I take it to be self-evident that the control of movement is sovereignty, since movement is life, and cessation of movement is death. Also the Supreme Court have recognized the practical correctness of this definition in Crandall *v.* Nevada, 6 Wall., 44. In that case the Court, having observed that the federal government had necessarily the power to transport troops throughout the Union, went on to declare that if this right were "dependent in any sense, however limited, upon the pleasure of a State, the Government itself may be overthrown by an obstruction to its exercise." And as a corollary to this decision, the same tribunal held in In re Debs, 158 U. S., 564, that the government, "by the very terms of its being," had the power, and was under the obligation to protect movement, by occupying the national

highways with the army, if necessary, should they be obstructed.

Therefore the construction and defence of the arteries through which the life of nations flows is now, and has ever been, the first and crucial task of government. Failing here, organized society must collapse. But highways and the movement upon highways can only be controlled by force, and, in modern times, governments have been classified according to the source whence the force they exercise is drawn. Where the force which dominates movement inheres in the sovereign, as in a conqueror, we call the government absolute, and, it may be, arbitrary. Where force is delegated to the sovereign by common consent, we call the government constitutional or popular. Nevertheless no government by consent can exist whose subjects are not persuaded that the sovereignty delegated by them to government is a sacred trust, to be executed by government as an agent for the common welfare. If the powers of sovereignty are prostituted to private use, privilege must supervene, confidence in the trust must die, and coercion must replace willing submission.

Conversely, sovereigns ruling by inherent force, tend, because they are not accountable, to use their power selfishly, whether sovereignty be lodged in an autocrat, an oligarchy, or a dominant race. Slavery is only an extreme form of unaccountable sovereignty. Examples throng upon the mind. When, under the Republic, the Romans conquered a country, some rich senator like Brutus or Appius Claudius would obtain an appointment as proconsul to administer the province; and one of the most famous passages in ancient literature is the page in the life of Lucullus in which Plutarch has described the fate which overtook a subject people, whose sovereign raised taxes, not for a public but for a private use. Having exhausted all else the people had, their bodies were sold into slavery. Equally striking is the letter which Cicero wrote to Atticus when journeying

through Asia as proconsul, in which he recounted how he followed the trail of his predecessor Appius Claudius as he would the trail of a monster, "of I know not what wild beast."

The old czars of Russia, when sending an official to act as their viceroy, used this formula, "Live off thy place and satisfy thyself." The formula has been abandoned, but the practice survives. Russian officials now, as heretofore, convert the taxes they collect to a private use. Hence the anarchy of Russia.

The methods of men like Appius Claudius made Cæsar a deliverer, and his conquest of the Republic a blessing to untold millions. The Empire was administered according to law, and taxes were devoted to a public use. Hence the Empire survived for ages. It is not the name by which a government is known which makes it beloved by its subjects, but the integrity with which the trust is enforced which the sovereign holds for the common welfare.

For upwards of eight hundred years the supreme effort of our race has been to change a social condition equivalent to that of a Roman province under the Republic, or of some outlying region of Russia now, into one where the sovereign powers of the State should be held as a trust for the common welfare, and where the trustee should be made accountable to the people, who are the *cestui que trust.* This struggle began with the battle of Hastings.

In 1066, after his victory, William the Conqueror established an arbitrary government in England, based upon wholesale confiscation of the property of the weak. He evicted the owners of the soil and divided the kingdom among his followers, making the knight's fee the military unit. The feudal system was a code of military law, and justice was dispensed, as between private litigants, by an appeal to force, trial being by combat.

The army thus became in theory self-supporting, the Crown being supposed to have reserved to itself property

enough to defray the ordinary costs of administration. In practice additional revenue was always needed, and this revenue was raised by arbitrary taxation. A famous example of William's taxation was the first great seizure of property under the power which we now call eminent domain.

A taking under eminent domain is only a tax levied exclusively upon one or more individuals. We now distribute this cumulative tax by compensating the sufferer, but it always remains a tax. Perhaps the best statement ever made of the relation of eminent domain to taxation occurs in the People *v.* Mayor of Brooklyn, 4 N. Y., 423, 424.

"Taxation exacts money, or services, from individuals, as and for their respective shares of contribution to any public burden. Private property taken for public use, by right of eminent domain, is taken not as the owner's share of contribution to a public burden, but as so much beyond his share. Special compensation is therefore to be made in the latter case because the government is a debtor for the property so taken; but not in the former because the payment of taxes is a duty and creates no obligations to repay, otherwise than in the proper application of the tax."

Hence any taking of private property by the sovereign must be a form of taxation; the only question in regard to the tax is whether the taking has been equitable, and whether the application of the avails has been to a public or a private use. Now we designate an unequal taking, without compensation, as confiscation, and the application of public funds to private use as peculation, but it was not always so, or even according to the common law; and this brings us to a condemnation of land under the Norman dynasty.

In 1079 William the Conqueror began the creation of the New Forest. To form this domain he condemned a large territory, paying no compensation, apparently, to land owners. The tradition is that he laid waste sixty villages. This has been doubted, but, whatever he did, he did enough to rouse

a hate whose memory has lasted until our own day. What he took he devoted exclusively to his own private use.

Substantially similar processes prevailed, whenever money was needed by an English sovereign, for about one hundred and fifty years. The chronicles are filled with the tales of the horrors of the reign of Stephen, of the robberies of Richard, and of the outrages of John. The nobles were exiled and their castles seized; the rich were imprisoned and tormented; the towns were deprived of the charters they had bought, and were forced to buy their privileges anew. At length, in 1215, the climax was reached: the whole nation united; the barons marched to London; on May 24 the city opened its gates, and on June 15 King John set his seal to that great instrument which put the sovereignty of England in trust. There can be no doubt or quibble as to the legal force of Magna Charta. It was a deed of trust, in the form of a contract between the King and the people, in which the King, in consideration of retaining the allegiance of his subjects, covenanted to hold the powers of sovereignty to a public use.

Amidst a vast array of authorities I quote from Bishop Stubbs:

"The Great Charter, although drawn up in the form of a royal grant, was really a treaty between the king and his subjects; it was framed upon a series of articles drawn up by them, it contained the provision usual in treaties for securing its execution, and although in express terms it contained only one part of the covenant, it implied in its whole tenor the existence and recognition of the other. The king granted these privileges on the understanding that he was to retain the allegiance of the nation. It is the collective people who really form the other high contracting party in the great capitulation. . . .

"In every case in which the privilege of the simple freeman is not secured by the provision that primarily affects

the knight or baron, a supplementary clause is added to define and protect his right; and the whole advantage is obtained for him by the comprehensive article which closes the essential part of the charter.

"This proves, if any proof were wanted, that the demands of the barons were no selfish exaction of privilege for themselves; it proves with scarcely less certainty that the people for whom they acted were on their side. The nation in general, the people of the towns and villages, the commons of later days, . . . had now thrown themselves on the side of the barons." Constitutional History of England, vol. 1, p. 530.

From the sealing of Magna Charta until now, English and American constitutional history has consisted of little else than the story of the effort of the people, on the one side, to enforce their trust, and of that of the class which has happened momentarily to be dominant, on the other, to escape from the terms of the pledge. And it is a noteworthy fact that the cause which we, as American citizens, have been taught to call the cause of liberty and of equal rights, has owed more to the courage of the soldier than to the wisdom of the judge. In moments of crisis in the long career of the English-speaking race, the courts have inclined toward the dominant class, and these judicial decisions have sometimes been corrected by the mandates of legislative assemblies, it is true, but sometimes also by the swords of champions like Cromwell, William III, and Washington. Thus we have come to view our greatest constitutional triumphs, not from the standpoint of the lawyers who sustained privilege, but from the standpoint of the men who fought the battles of rebellion for equality.

In 1629, upon information against him, the Court of the King's Bench imprisoned Sir John Elliot in the Tower, for words spoken in debate; and in the Tower he died. In 1638 the Court of Exchequer Chamber gave judgment against

John Hampden in the case of the Ship Money. In 1682, to aid Charles II in bringing Algernon Sidney to the block, the Chief Justice of England held that when Sidney, in the solitude of his chamber, wrote down his thoughts on government, he committed an overt act of treason. In 1686, in the case of Sir Edward Hales, Chief Justice HERBERT, in the name of all the judges save one, thus defined the binding force of Magna Charta, saying, in substance, that the kings of England are absolute sovereigns; that the laws of England are the King's laws; that the King has power to dispense with any of his laws as he sees necessity for it; that the King is the sole judge of that necessity, and that this is not a trust invested in or granted to the King by the people, but the ancient sovereign power and prerogative of the kings of England, which never yet was taken from them, nor can be by Parliament or any human means. 11 Howell's State Trials, 1165–1198. Godden *v.* Hales, 2 Shower, 475.

In 1761 the Superior Court of Judicature of the Province of Massachusetts Bay sustained the Crown in the case of the Writs of Assistance,—writs which were to be issued with the object of collecting taxes from the people, whose proceeds were not to be held in trust for the common welfare.

In 1856, in Dred Scott *v.* Sandford, the Supreme Court of the Union held that no man whose ancestors had been sold into slavery in America could become a citizen of the United States.

Prerogative may be defined as the latitude which the kings of England arrogated to themselves in the discharge of their trust. As this latitude was extended by construction to the length of dispensing with all the restraints of law, disputes raged touching the limits within which it might be confined. I pass over the Middle Ages to come at once to the civil wars of the seventeenth century, from which all our modern legal theories spring.

When the Stuarts came to the throne in 1603, the old

feudal baronage had passed away, and had been replaced by an aristocracy singularly inapt as soldiers. This aristocracy was confronted with a martial race of farmers, and it soon became evident that if they were to convert the powers of sovereignty to their private use, their agent, the King, would need a standing army organized by professional officers. To obtain the revenue for such an army, arbitrary taxation had to be imposed. Hence the collection of the ship money and the resistance of Hampden. After the King's Bench had sustained the Crown against Hampden, nothing remained but submission, or the coercion of the trustee. The people of England chose coercion; and, having defeated the King in battle, they imprisoned and tried him for treason, on the charge that he had broken the public trust.

The charge brought against the King by the Commons declared that "Charles Stuart, being admitted King of England, and therein trusted with a limited power to govern by and according to the laws of the land, and not otherwise, and by his trust, oath and office, being obliged to use the power committed to him, for the good and benefit of the people, and for the preservation of their rights and liberties; yet nevertheless" he had committed divers crimes "for the advancement and upholding of a personal interest of will and power, and pretended prerogative to himself and his family, against the public interest, common right, liberty, justice, and peace of the people of this nation, by and for whom he was intrusted as aforesaid." Having been found guilty, the King was sentenced to death on January 29, 1649. 4 Howell's State Trials, 1070–1072.

Nor was this all. Two classes who sought to prostitute sovereignty to private ends conspired together to wage war with Charles. These classes were the nobility and the clergy. Among the King's counsellors Thomas Wentworth, Earl of Strafford, represented the nobility, William Laud, Arch-

bishop of Canterbury, the clergy; and both of these conspirators against the common right were beheaded on Tower Hill.

Cromwell's victories settled forever the question as to the power of the people to coerce the Crown, should the people arm; therefore physical force was not again invoked by the privileged classes. It remained, however, possible for the trustee to corrupt the assembly which represented the people, by the use of public money. The theory of the "divine right" was not abandoned. The issue turned upon the extent to which the courts and the House of Commons could be controlled by the conversion of public property to private use. The judiciary fell easily. The test case I have already cited. It was that of Sir Edward Hales, who had been appointed Lord Lieutenant of the Tower without taking the oaths required by statute. Hales pleaded that he had been dispensed from taking the oaths by letters patent; and the Court, speaking through Chief Justice HERBERT, held, in 1686, that the King was the agent of God, and not of the people, and could be bound by no human law. Thereupon the people of England ejected James II from the kingdom, and raised William and Mary to the throne by act of Parliament, passing at the same time the Declaration of Right, which is a reaffirmation of Magna Charta and an elaboration of the trust. This declaration of trust the new King and Queen solemnly promised to observe.

In 1689 Locke, in answer to Filmer, laid down the two great fundamental propositions of constitutional government: 1st, That the powers of sovereignty cannot be bartered away; 2d, That they are inherent in the people, and must be held by the agents of the people, as their trustees, for the common welfare.

"The legislative or supreme authority cannot assume to itself a power to rule, by extemporary, arbitrary decrees; but is bound to dispense justice, and to decide the rights of

the subject, by promulgated, standing laws, and known authorized judges. . . .

"To this end it is that men give up all their natural power to the society which they enter into, and the community put the legislative power into such hands as they think fit; with this trust, that they shall be governed by declared laws, or else their peace, quiet, and property will still be at the same uncertainty, as it was in the state of nature."

In other words a government of consent will be replaced by a government by force.

"The legislative [authority] cannot transfer the power of making laws to any other hands: for it being but a delegated power from the people, they who have it cannot pass it over to others. . . .

"These are the bounds which the trust that is put in them by the society, and the law of God and nature, have set to the legislative power of every Commonwealth, in all forms of government.

"First, They are to govern by promulgated established laws, not to be varied in particular cases, but to have one rule for rich and poor, for the favourite at court, and the countryman at plough.

"Secondly, These laws also ought to be designed for no other end ultimately, but the good of the people.

. . . . . .

"Fourthly, the legislative neither must nor can transfer the power of making laws to any body else, or place it anywhere, but where the people have."

Of Civil Government, §§ 136, 141, 142.

With the Revolution of 1688 the principles of the accountability of the King as trustee became too firmly established to be disputed; but the Crown was rich, and no machinery existed by which the use of the public property intrusted to the Crown for safe keeping could be regulated. By 13

William III, c. 2, the commissions of the judges were made to run during good behavior, instead of during pleasure, but the change of tenure, which in effect dated from the opening of this reign, does not appear to have greatly altered the tendency of the courts to sustain private vested interests at the expense of the public. The income which Charles II held in his own right, from Crown domains and from other sources, may have amounted to about £1,400,000 a year, a sum equal, perhaps, to six times its nominal value now, and this sum, and the capital it represented, the King claimed the right to dispose of as he pleased. The question came before the courts for adjudication in the so-called Bankers' Case, Skinner, 601.

In 1672 Charles II, having borrowed a large sum from the London bankers, as we should say, on demand, gave notice that he should decline to pay the principal, and that creditors of the Crown must be content with interest made payable out of the hereditary excise.

In 1695 the lawfulness of such an alienation of public property without an act of Parliament was disputed, but Lord HOLT held that "The King was seized of this revenue in fee, to which estate a power to alien or change is annexed by the law. . . . And it is no objection that they are given under a trust. . . .

"And as to the objection, that if the King has such a power to alien the inheritance of the Crown, that this will be prejudicial, and he might infeeble the realm, and waste the revenues of the Crown by lavish and profuse grants of it; he answered that such a dishonorable thing ought not to be supposed of the King to whom the law attributes so much power and dignity; and to restrain the King from such a power, is absurd, and against the constitution of the realm."

Notwithstanding Lord HOLT'S views as to the integrity of the King in his capacity of trustee of the public funds, William III gave so profusely to his Dutch favorites that,

in the first year of Anne, Parliament passed an act which, having recited that "whereas the necessary expenses of supporting the crown, or the greatest part of them, were formerly defrayed by a land revenue, which hath . . . been impaired and diminished by the grants of former kings and queens . . . so that her Majesty's land revenues at present can afford very little toward the support of her Government," enacted that no grant should be made of Crown lands for more than thirty-one years.

This statute could produce only slender results so long as the public trustee had the means of alienating the public funds without rendering an account. It mattered little whether the alienation was in fee or for years.

The King and the party supporting him had the supreme object in view of controlling the powers of sovereignty for their private ends, and to accomplish his purpose George III shrank from no personal sacrifice. George III enjoyed a net income, entirely at his own disposal, of about £1,000,000. Besides this he inherited £172,000, saved by his father. Yet he lived penuriously. "The royal household," Burke said, "has lost all that was stately and venerable in the antique manners, without retrenching anything of the cumberous charge of a Gothic establishment."

"In all this the peoople see nothing but the operations of parsimony, attended with all the consequences of profusion. Nothing expended — nothing saved. . . . They do not believe it to be hoarded, nor perceive it to be spent." Furthermore, the King was always in debt. In 1769 he asked the Commons for £513,000 to pay the arrears of his Civil List when he had been but nine years on the throne. And he did this at a moment when his government was odious because of the prosecution of Wilkes. At the same time his ministers had to refuse all explanations, and decline to submit any account, for the whole of this great public treasure had been spent on bribing those who were public trustees as much

as was the King himself. Lord HALIFAX defined a bribe as money paid "for a particular job; a pension is a constant, continual bribe." The King's Gothic household was a mass of sinecures, used as pensions, and the power of his army of political cooks and scullions was so great that nothing could prevail in Parliament against him, so long as the methods he used were concealed. One of the most famous passages in Burke's works occurs in his speech made in 1780 on "Economical Reform," in which he described how Lord TALBOT tried to reorganize the royal kitchen.

"Lord Talbot attempted to reform the kitchen. . . . On that rock his whole adventure split. His whole scheme of economy was dashed to pieces; his department became more expensive than ever; the Civil List debt accumulated. Why? It was truly from a cause, which, though perfectly adequate to the effect, one would not have instantly guessed. It was because the *turnspit in the King's kitchen was a member of Parliament.* The King's domestic servants were all undone; his tradesmen remained unpaid and became bankrupt — *because the turnspit of the King's kitchen was a member of Parliament.* . . . The judges were unpaid; the justice of the kingdom bent and gave way; the foreign ministers remained inactive and unprovided; the system of Europe was dissolved; the chain of our alliances was broken; all the wheels of government at home and abroad were stopped — *because the King's turnspit was a member of Parliament.*"

With the trustee possessing an unlimited power of bribing those who should audit his accounts, enforcement of the public trust was impossible, unless the methods employed by all concerned could be subjected to unrestricted criticism. Every vested interest, therefore, from the King on the throne to the King's turnspit in Parliament, wrought desperately to suppress publicity, and none wrought harder than the judges on the bench. The test case came before Lord MANSFIELD in the prosecution of Woodfall for the publication of the letter

of Junius to the King. According to Star Chamber precedents Lord MANSFIELD ruled that malice in libel was matter of law for the Court, and that the province of the jury was confined to finding the publication of the written words with the truth of the innuendos. Rex *v.* Woodfall, 5 Burrow, 2661. Had Lord MANSFIELD prevailed the press would have been muzzled, and there could have been no enforcement of the public trust; but the jury declined to follow his instructions, and found the renowned verdict of "guilty of printing and publishing only," upon which no judgment could be entered. In the next prosecution the verdict was "not guilty." Thus publicity was secured. In 1792 came Fox's libel act, in 1832 the reform of Parliament, and, as a consequence, during the reign of Victoria, all the public property of the British people has been placed in strict trust. The Civil List was settled at £385,000 a year, and there have been no debts. Burke proposed, as a radical reform, that the Pension List should be limited to £60,000 annually; the Queen was restricted to £1200. In 1851 the Crown lands were vested in the Commission of Woods and Forests, and the net income derived from the property was turned over to the public revenue. In 1877 the New Forest, the private hunting ground of William the Conqueror, was conveyed to trustees for public use as a park.

The enforcement of the public trust in England is now effected through a very perfect automatic adjustment for obtaining what amounts to a referendum. The care of public property is vested in various subordinate boards, but the responsible trustee is a committee chosen by the direct representatives of the people. This committee can be removed at pleasure by a vote of the House of Commons, under the limitation that the trustee may order a new election of the House so that the people may pass upon his administration of his trust.

The fundamental principle of such a system is the invio-

lability of the public trust. The *cestui* is the final and absolute arbiter of what shall be done with his own. No Parliament can bind a successor; no agent, in or out of Parliament, can, by treachery or incompetence, put the people, who are the principal, at an irremediable disadvantage. The sovereign powers of the nation can never be bartered away.

The English have left their constitutional law thus fluid because their confidence in legislatures has not been impaired.

In England the struggle to enforce the trust lay between the Commons and the privileged classes, at whose head stood the Crown. In America the attack upon the common right came rather from Parliament as a whole, that is, from King, Lords and Commons, than from any person, or class of persons in Great Britain. Consequently Americans conceived a fear of legislative assemblies and limited their agency by written instruments. The American Constitution is a strict deed of trust, but a deed only elaborating the ancient trust first declared in Magna Charta. Its scope is well defined in the preamble of the Constitution of Massachusetts.

"The body politic is formed by a voluntary association of individuals: it is a social compact, by which the whole people covenants with each citizen, and each citizen with the whole people, that all shall be governed by certain laws for the common good."

The written Constitution being a deed of trust the courts assumed the task of interpretation, and therefore it has devolved upon them to define what legislative acts conduce to the common welfare, and what acts transcend the limit of the trust. As I have already shown by the precedents, the tendency of courts is to support particular dominant interests at the public cost, and this soon proved to be as true in the United States as in England. During the first quarter of the last century the judiciary went far toward undermining the foundation upon which the common right must always rest. They held that American legislatures had

the power to alienate forever and beyond recall, in favor of private persons, not only public property held in trust for the whole people, but sovereignty itself. They held that legislatures could not only bind themselves and their successors forever to a remission of taxation, but that an ordinary charter of incorporation, such as a turnpike or railway charter, was a contract which could not be modified without the consent of the grantee.

Had the principle of constitutional law embodied in these early decisions been carried out logically to its legitimate end, I apprehend that the American people must long since have fallen into abject servitude to monopoly, or a revolution must have ended an intolerable situation. As I shall presently show, these decisions have not been followed. Every effort has been directed to minimize their effect, but the bias they have given to American thought is reflected in the pretensions advanced by these defendants, pretensions which, I conceive, could not be advanced in any other country where constitutional government prevails.

To present to this tribunal any coherent view of the modern law, I must go at some length into this phase of our constitutional history.

After the Revolution and during the Confederation extreme poverty and, in consequence, some disorder prevailed in the United States. A movement began to repudiate debts, and the Constitution of the United States was the result, to a certain degree, of an effort of vested interests to protect themselves. Hence the insertion, among other limitations upon the power of the States, of the clause forbidding any State to impair the obligation of contracts.

The judges were generally appointed during this period of violent reaction, and, besides, their minds were tinged with the fear of anarchy engendered by the French Revolution. The effect became manifest almost from the organization of the Supreme Court, but the first far-reaching decision

was not rendered until almost twenty-five years after the establishment of the new government.

In 1812, in New Jersey *v.* Wilson, 7 Cranch, 164, Chief Justice MARSHALL held that, under the tenth section of the first article of the Federal Constitution, which forbids any State to impair the obligation of a contract, a State legislature might bargain away, in favor of a private individual, its power of taxation, and that this bargain would be binding forever upon the whole people, unless the Constitution of the United States should be changed. That is to say, the Supreme Court held that it lay in the power of the trustee to so use his agency as to annihilate the *cestui que trust.* For the Chief Justice was the first to admit that no community could survive which could not tax, and he seemed prepared to set no limit to the exercise of this power of alienation of taxation, if it existed at all. Such was the logical inference to be drawn from this decision. Though there has been unremitting protest against the doctrine of New Jersey *v.* Wilson, it has never been overruled; it has, however, been explained.

In 1819 the Court took the next step in the Dartmouth College Case, in which Chief Justice MARSHALL decided that a charter of incorporation, granted to a business enterprise, was a contract which could not be modified without the consent of the grantee. In sustaining the argument of Webster, the Chief Justice said:

"Are contracts of this description [corporate charters] of a character to excite so little interest, that we must exclude them from the provisions of the Constitution, as being unworthy of the attention of those who framed the instrument? Or does public policy so imperiously demand their remaining exposed to legislative alteration, as to compel us, or rather permit us, to say that these words which were introduced to give stability to contracts, and which in their plain import comprehend this contract, must yet be so construed as to

exclude it." Trustees of Dartmouth College *v.* Woodward, 4 Wheat., 645.

New Jersey *v.* Wilson and Dartmouth College *v.* Woodward are decisions substantially in line with Lord HOLT'S in the Bankers' case, and as, after Lord HOLT'S decision, it became imperative upon the English people to undo the work which he had done, so after 1820 the American people addressed themselves to averting the consequences which it became evident were likely to ensue from this breach in the sanctity of the public trust. Not only did many States so amend their constitutions as to forbid their legislatures from granting unlimited charters, but all took means to avert such a catastrophe, and now, the granting of a charter, without the reservation of the right to alter or revoke, would be taken as presumptive evidence of corruption.

The Supreme Court itself felt the necessity of receding, and no more striking description of the chasm on the brink of which this country then stood poised is to be found in any book than in Chief Justice TANEY'S opinion in The Proprietors of Charles River Bridge *v.* The Proprietors of Warren Bridge, 11 Peters, 420, argued in 1837, eighteen years after the Dartmouth College case. The effect is heightened if this opinion be read in connection with that of STORY, J., which follows, in which STORY indicates the length to which the Court as it had formerly existed was prepared to go.

Sixteen years later, in 1853, in Ohio Life Insurance Co. *v.* Debolt, 16 How., 416, Chief Justice TANEY approached the limit of what could be done without absolutely overruling his predecessor. He there insisted upon the great fundamental truth, that the powers of sovereignty are an indefeasible trust which cannot be bargained away, since they are essential to the life of the State.

"The powers of sovereignty confided to the legislative body of a State are undoubtedly a trust committed to them, to be executed to the best of their judgment for the public

good; and no one legislature can, by its own act, disarm their successors of any of the powers or rights of sovereignty confided by the people to the legislative body, unless they are authorized to do so by the constitution under which they are elected." 16 How., 431.

From the day of the decision of the Dartmouth College case until now, in proportion as the corporate interests which seek to make sovereignty subservient to their private ends have gathered volume, so has the determination of the people to defend the public trust found expression not only in legislation, but in judicial decisions. I can illustrate this movement no better than by citing the strained construction which the courts have given to the doctrine of eminent domain to distinguish it from taxation, and to save it unimpaired for the people.

As I have already shown, nothing can be clearer as an economic proposition than that eminent domain is only one of the manifold ways in which taxation may be imposed. As the Supreme Court said in Pollard's Lessee *v.* Hagan, 3 How., 223, when quoting Vatel, eminent domain is "the right which belongs to the society, or to the sovereign, of disposing, in case of necessity, and for the public safety, of all the wealth contained in the State."

This is nothing but a definition of taxation, for a tax or an impost is any contribution taken from the subject by the sovereign by force. Singer Manfg. Co. *v.* Heppenheimer, 58 N. J. Law, 633.[1] In 1812 MARSHALL, without hesitation, decided that the State might bargain away its power to tax an individual for that individual's behoof; a couple of generations later the Massachusetts judiciary spoke thus of eminent domain:

"It is an inherent element of sovereignty, and . . . must continue unimpaired in the State. . . . It cannot be abridged

[1] "The word 'imposition' includes every kind of enforced contribution to the public treasury." 58 N. J. Law, 638.

so as to bind future legislation. The franchise of a corporation is not exempt." Eastern R. R. Co. *v.* Boston & Maine R. R., 111 Mass., 131.

A great social gulf is reflected in the divergence between this case and Dartmouth College *v.* Woodward, and New Jersey *v.* Wilson.

Furthermore, if the powers of sovereignty are held in trust by legislatures for the public, so is public property. The public waters of the State, for example, are a trust held by the government for the common welfare.

"The law in this Commonwealth seemed to be settled by the case already cited, of Commonwealth *v.* Alger, 7 Cush., 65. There it is declared that by the common law of England, as it stood long before the settlement of this country, the title to flats was in the King, and that it was so held by him in trust for public uses." Commonwealth *v.* Roxbury, 9 Gray, 482.

And so it is with great ponds and lakes. They are property held in trust by the government for the public, and are to be used for the advancement of the public welfare.

"The plaintiffs contend that the charter of the Watuppa Reservoir Company operated as a grant to the company of the right to use and control the waters of the Watuppa Ponds for the purposes of power. . . . Whether it be construed as a revocable license or a grant of a vested right, the company took and holds its rights subject to the paramount right of the government to use the water for the public purposes for which it was held in trust." Watuppa Reservoir Co. *v.* Fall River, 147 Mass., 559, 560; Gardner Water Co. *v.* Inhabitants of Gardner, 185 Mass., 194; Milford Water Co. *v.* Hopkinton, 192 Mass., 497.

So land granted to a city for streets is held upon a public trust, and can be used for no other purpose.

"Assuming, however, that the proceedings under the act of 1813, . . . have the effect to vest in the city of New York

that indefeasible and entire title in fee to the streets, yet . . . . the grant is expressly upon trust, for a public purpose, that the lands may be appropriated and used forever as public streets. . . . The City has neither the right nor the power to apply any such property to other than public uses, and those included within the objects of the grant." People *v.* Kerr, 27 N. Y., 197.

And this interpretation of the indefeasible duty of the government to act as trustee for the people has been carried so far that it has been held that public property bought by a city with taxes, such as a park or a library, or acquired by gift, as a museum, cannot be taken away by the State without compensation, although the city be but an agent of the government for administering a certain portion of the territory of the State. Mt. Hope Cemetery *v.* Boston, 158 Mass., 519, 521.

Advancing logically from premise to conclusion in this line of reasoning, the deduction has been forced upon the judiciary that, if the governments of our States hold public property in trust for the welfare of the whole people, they cannot act beyond the scope of their agency, and therefore that they cannot convey away such property to the public injury. A breach of trust of this character arose from a grant made by the State of Illinois to the Illinois Central Railroad.

The facts were these: The State of Illinois conveyed to the Illinois Central Railroad the flats beneath the waters of Lake Michigan which formed the harbor of Chicago. This grant, in the words of the Court, converted a railway company into a corporation to manage and control "the harbor of Chicago, not simply for its own purpose as a railway corporation, but for its own profit generally." 146 U. S., 451. Hardly had the act taken effect before it became evident that the situation was intolerable, and that the people would have to regain control of their harbor, or else that

the city would be ruined. Accordingly, the State undertook to resume its grant, and the railway claimed compensation. But to be obliged to pay compensation for the flats would have been almost as bad as to have lost possession, for the value of these flats represented, in substance, something like the rental value of Chicago itself. If, however, the legislature had the power to contract, under the decisions of the courts the people were bound by its agency, and there was no redress. Confronted with this emergency, the Supreme Court thus laid down the law relating to the obligation of the public trust:

"That the State holds the title to the lands under the navigable waters of Lake Michigan, within its limits, in the same manner that the State holds title to soils under tide water, by the common law, we have already shown, and that title necessarily carries with it control over the waters above them whenever the lands are subjected to use. But it is a title different in character from that which the State holds in lands intended for sale. It is different from the title which the United States hold in the public lands which are open to preëmption and sale. It is a title held in trust for the people of the State that they may enjoy the navigation of the waters, carry on commerce over them, and have liberty of fishing therein freed from the obstruction or interference of private parties. The interest of the people in the navigation of the waters and in commerce over them may be improved in many instances by the erection of wharves, docks and piers therein, for which purpose the State may grant parcels of the submerged lands; and, so long as their disposition is made for such purpose, no valid objections can be made to the grants. It is grants of parcels of lands under navigable waters, that may afford foundation for wharves, piers, docks and other structures in aid of commerce, and grants of parcels which, being occupied, do not substantially impair the public interest in the lands and waters remaining,

that are chiefly considered and sustained in the adjudged cases as a valid exercise of legislative power consistently with the trust to the public upon which such lands are held by the State. But that is a very different doctrine from the one which would sanction the abdication of the general control of the State over lands under the navigable waters of an entire harbor or bay, or of a sea or lake. Such abdication is not consistent with the exercise of that trust which requires the government of the State to preserve such waters for the use of the public. The trust devolving upon the State for the public, and which can only be discharged by the management and control of property in which the public has an interest, cannot be relinquished by a transfer of the property. The control of the State for the purposes of the trust can never be lost, except as to such parcels as are used in promoting the interests of the public therein, or can be disposed of without any substantial impairment of the public interest in the lands and waters remaining." Illinois Central Railroad Co. *v.* Illinois, 146 U. S., 452.

"The State can no more abdicate its trust over property in which the whole people are interested, like navigable waters and soils under them, so as to leave them entirely under the use and control of private parties, except in the instance of parcels mentioned for the improvement of the navigation and use of the waters, or when parcels can be disposed of without impairment of the public interest in what remains, than it can abdicate its police powers in the administration of government and the preservation of the peace. In the administration of government the use of such powers may for a limited period be delegated to a municipality or other body, but there always remains with the State the right to revoke those powers and exercise them in a more direct manner, and one more conformable to its wishes. So with trusts connected with public property, or property of a special character, like lands under navigable

waters, they cannot be placed entirely beyond the direction and control of the State." Illinois Central Railroad Co. *v.* Illinois, 146 U. S., 453.

This case elucidates the American system of enforcing the public trust. In England, had Parliament made such a grant, the act would probably have led to a vote of want of confidence, to a dissolution, and a referendum. In America the referendum was impossible, for the contract, if lawful, was irrevocable. The only alternative was to appeal to the courts to declare the act a breach of trust and void. And the Court in this instance held that, "Any grant of the kind is necessarily revocable, and the exercise of the trust by which the property was held by the State can be resumed at any time." 146 U. S., 455.

On the other hand, this principle cuts deep into the legislative discretion in providing for the public welfare. And this the minority of the Court pointed out: "The opinion of the majority, if I rightly apprehend it, likewise concedes that a State does possess the power to grant the rights of property and possession in such lands to private parties, but the power is stated to be, in some way restricted to 'small parcels, or where such parcels can be disposed of without detriment to the public interests.' . . . But it is difficult to see how the validity of the exercise of the power, if the power exists, can depend upon the size of the parcel granted. . . .

"It would seem to be plain that, if the State of Illinois has the power, by her legislature, to grant private rights and interests in parcels of soil under her navigable waters, the extent of such a grant and its effect upon public interests . . . are matters of legislative discretion." Dissenting opinion by SHIRAS, J., 146 U. S., 467.

The difficulty with the argument of Mr. Justice SHIRAS is that it ignores the vital distinction, drawn by the cases of New Jersey *v.* Wilson and of Dartmouth College, between the American and the English constitutional system. The

legislative discretion may legitimately be left unhampered, if it be conceded that no legislature can bind its successor; but if legislatures may bargain away public property, and even sovereignty, for the benefit of private persons, the public trust must eventually be annihilated, or there must be some tribunal to revise the contracts of the trustee. That the situation has put the courts in a false position toward the public has been [illegible] admitted repeatedly by the judiciary. The language [illegible] in many of the tax cases is [illegible] striking. I quote [illegible] from one of them, decided [illegible] in which the Supreme Court frankly confesses that [illegible] predicament is [illegible] that, having gone too [illegible] the only [illegible] to them is to restrict [illegible] of these decisions [illegible] may be:

[illegible] manifest that [illegible] which it is claimed re- [illegible] species of property [illegible] due proportion of the [illegible] of government [illegible] so clear that there [illegible] about its terms. [illegible] and is inherent [illegible] presumption in [illegible] better for the [illegible] should on no [illegible] that the [illegible] limita- [illegible] a con- [illegible] ation, [illegible] how- [illegible] is a [illegible] this [illegible]

[illegible] s, [illegible] ay [illegible] rel- [illegible] ect. [illegible] neral [illegible] ance, [illegible] to the [illegible] motion [illegible] by the [illegible] ich taxa- [illegible] character [illegible] determine [illegible] tude of the [illegible] the general [illegible] iblic welfare, [illegible] on. [illegible] idamental. It [illegible] a reason rather

repudiation by Massachusetts of Chief Justice SHAW'S celebrated constitutional theory that eminent domain might be granted to private individuals to increase the prosperity of a private enterprise.

In 1853 the manufacturing interests of Massachusetts had become predominant, and their influence was strong enough with the legislature to enable manufacturing companies to obtain grants of the right of eminent domain in order to obtain their water power. In Hazen *v.* Essex Co., 12 Cush., 475, the constitutionality of such a grant came before the Supreme Court of the Commonwealth. In that case the Chief Justice went to great lengths in support of the legislative discretion:

"The establishment of a great mill power for manufacturing purposes, as an object of great public interest, especially since manufacturing has come to be one of the great public industrial pursuits of the Commonwealth, seems to have been regarded by the legislature . . . and, in our judgment, rightly so, in determining what is a public use, justifying the exercise of the right of eminent domain." 12 Cush., 478.

Six years later the Essex Company was indicted for maintaining a nuisance, in the shape of a dam which obstructed the run of fish. Then SHAW emphasized his former decision by declaring that, "The objects proposed to be accomplished by the defendants were so far public in their nature, and designed to promote the public benefit, that it was quite competent for the legislature to exercise the power of eminent domain, by authorizing them to take private property when necessary." Commonwealth *v.* Essex Co., 13 Gray, 249.

These decisions of Chief Justice SHAW seem to have marked the close of the period at which private trespasses upon sovereignty have been explicitly tolerated as constitutional by the American judiciary. About 1870 a new phase of

constitutional construction appears to have opened, the proximate cause for which probably was the scandals connected with the organization of the Union Pacific Railroad. In 1873, in the face of a heavy public disaster, the Supreme Court of Massachusetts took occasion to go to the root of the responsibility of government to the people, as their trustee. In 1872 the great fire of Boston occurred, and the legislature authorized the issue of bonds to aid private persons in rebuilding. The Court held this legislation bad, as being an appropriation of public money to a private use.

"The power to levy taxes is founded on the right, duty and responsibility to maintain and administer all the governmental functions of the State, and to provide for the public welfare.

"To justify any exercise of the power requires that the expenditure which it is intended to meet shall be for some public service, or some object which concerns the public welfare. The promotion of the interests of individuals, either in respect of property or business, although it may result incidentally in the advancement of the public welfare, is, in its essential character, a private not a public object. However certain and great the resulting good to the general public, it does not, by reason of its comparative importance, cease to be incidental. The incidental advantage to the public, or to the State, which results from the promotion of private interests . . . does not justify their aid by the use of public money raised by taxation, or for which taxation may become necessary. It is the essential character of the direct object of the expenditure which must determine its validity, as justifying a tax, and not the magnitude of the interests to be affected, nor the degree to which the general advantage of the community, and thus the public welfare, may be ultimately benefited by their promotion.

"The principle of this distinction is fundamental. It underlies all government that is based upon reason rather

than upon force. . . . There are, indeed, many cases in which the sovereign power of government is exercised to affect private rights of property in favor of private parties, either individuals or corporations. Most conspicuous among these are turnpikes and railroads; in whose favor this right of eminent domain is frequently exercised. Private rights are thus taken and transferred, not to the State, but to the private corporation; and the compensation to the persons injured, required by the Constitution, is also rendered from the corporation. Such an appropriation of property is justified, and can only be justified, by the public service thereby secured in the increased facilities for transportation of freight and passengers, of which the whole community may rightfully avail itself. The franchises of the corporation are held charged with this duty and trust for the performance of the public service, for which they were granted." Lowell *v.* Boston, 111 Mass., 460, 461, 463.

Twenty years later, in Turner *v.* Nye, 154 Mass., 579, the Supreme Court of Massachusetts admitted that grants of the power of eminent domain like that sanctioned in Hazen *v.* Essex Co. could not be sustained as law.

Precisely similar is the opinion of the justices of the Supreme Court of Maine, on the question as to whether the legislature could authorize towns to loan money to manufacturers.

"If it were proposed to pass an act enabling the inhabitants of the several towns by vote to transfer the farms or the horses or oxen, or a part thereof, from the rightful owner or owners to some manufacturer whom the majority might select, the monstrousness of such proposed legislation would be transparent. But the mode by which property would be taken from one or many and given to another or others can make no difference in the underlying principle. It is the taking that constitutes the wrong, no matter how taken. . . .

"It would simply be an act of despotic power to sequestrate the property of an individual or individuals directly or indirectly by the means of taxation, for the purpose of giving it away against the will of the owner, and to those whom others than he may select." 58 Maine, 593, 595.

I now come to the core and heart of all government. It lies in that indefinite power which the courts have called the *Police Power*, but which is in truth that essential, inherent, and indefeasible right which is defined in the preamble to the Constitution of the United States as the power to "establish justice, insure domestic tranquillity, provide for the common defence, promote the general welfare, and secure the blessings of liberty to ourselves and our posterity."

As this power is the heart of government, so is the control of the highways the heart of this power. The regulation of highways falls under the head of the *Police Power*, Munn *v.* Illinois, 94 U. S., 125, and that power can neither be alienated, diminished, nor used to the public detriment. It is a sacred trust which government holds for the whole people for the common welfare, and any violation of this trust is void. I quote the following singularly energetic passage from a decision of the Supreme Court of Maine touching the inherent power of the community to regulate its highways:

"The State may in some cases forego the right to taxation, but it can never relieve itself of the duty of providing for the safety of its citizens. This duty and consequent power, override all statute or contract exemptions. The State cannot free any person or corporation from subjection to this power. All personal as well as property rights must be held subject to the police power of the State." Boston & Maine R. R. *v.* County Commissioners, 79 Maine, 393.

Nor is this mutual relation between sovereign and subject peculiar to any age, to either hemisphere, or to any form of government. In despotism or republic it is the same, for

it is the ultimate necessity of self-preservation. If we go back to the very dawn of history we shall find that the maintenance and protection of the ways has ever been the chief function of the sovereign, for it is to guard the ways that armies and navies are organized; while, on the other hand, the cost of the maintenance and protection of the ways is a tax or impost upon the people. It matters not how this contribution for the building and maintenance of the ways has been collected; it has always been, and is to-day, a tax or impost; that is to say, an involuntary contribution exacted from the people by the sovereign for a public purpose. Hancock *v.* Singer Manfg. Co., 62 N. J. Law, 334.

Sometimes, as with the Romans, highways have been built and maintained by the government, and the cost has been met by a direct tax; sometimes, as under the French monarchy, highways have been built and cared for by the labor of a servile class, and this gratuitous toil the highest of French authorities defined as an unjust and iniquitous, because an unequal, impost. Edit du Roi, Qui supprime les Corvées, Œuvres de Turgot, Paris, 1809, vol. 8, p. 287. Sometimes the cost of maintenance has been defrayed by fees, as with harbor dues, which are taxes. Southern S. S. Co. *v.* Portwardens, 6 Wall., 31. Sometimes by tolls, as with turnpikes, which tolls, in the words of the New York Court of Appeals, are "delegated taxation." The People *v.* Mayor, etc., of Brooklyn, 4 N. Y., 431; and so likewise the Court of King's Bench has held in Bussey *v.* Storey, 4 B. & Ad., 109. Sometimes by special assessments upon abutters for improvements, as with modern betterments, which are taxes. Spencer *v.* Merchant, 125 U. S., 345. And sometimes by seizure of private property for this public purpose, which seizure, being a tax, or a contribution exacted from the individual for a public work, did not necessarily imply a right to compensation at common law. Governor & Company of British Cast Plate Manufacturers *v.* Meredith *et al.*, 4 Term., 794.

The method by which the money is raised is immaterial; the essential point is that the funds necessary for the construction and maintenance of the avenues through which circulate the national life are a charge upon the people, and are met by an involuntary contribution, which, directly or indirectly, either by the sovereign himself, or by an agent of the sovereign, are used to maintain works without which the community would perish.

In the Middle Ages, when roads were bad, and travel by land was slow and dangerous, the chief highways were waterways, every stream which would float the smallest boat was utilized, and accordingly Magna Charta guaranteed that the public trust should cover rivers and harbors as well as the roads over which merchants had to pass.

As Lord HOLT held, in The King *v.* Clark, 12 Modern, 615, "To hinder the course of a navigable river is against Magna Charta, c. 23;" and long afterward the Court of King's Bench declared that landways were as much protected as waterways, for in Magna Charta it was provided that merchants might come and go by land or sea, and lawful men might leave the kingdom and return, save in time of war.

"Many of the King's rights are, to a certain extent, for the benefit of his subjects, and that is the case as to the sea, in which all his subjects have the right of navigation, and of fishing, and it is so in highways, along which all his subjects have the right of passage, and the King can make no modern grants in derogation of those rights." BAYLEY, J., in Blundell *v.* Catterall, 5 Barn. & Ald., 304.

"The dominion and property in navigable waters, and in the lands under them, being held by the King as a public trust, the grant to an individual of an exclusive fishery in any portion of it, is so much taken from the common fund intrusted to his care for the common benefit." Martin *v.* Waddell, 16 Peters, 411.

I submit, therefore, that, if any proposition of constitutional law is ever established, my proposition is established, that the care and maintenance of the public ways is an indefeasible trust of which the sovereign cannot divest himself, and that in return the sovereign has the right to impose taxes or imposts upon subjects for defraying the cost of those ways; but that these taxes and imposts are only lawful, in America, if they are levied for the purpose of defraying the cost of this public work, and that they cannot be used, directly or indirectly, for the undue emolument of individuals.

This difficulty, touching the unlawful diversion of the highway tax or impost from its legitimate object, arises usually in countries where the administration of the highways is delegated by the sovereign to an agent, precisely as the unlawful exaction of taxes usually occurs in jurisdictions wherein taxes are farmed; for the methods by which the sovereign may discharge his highway trust are almost as varied as the methods by which he may raise the money which defrays the cost thereof. Sometimes, as in Rome or modern Germany, the sovereign does the work himself, and collects his compensation therefor by direct taxes, or by tolls, or by railway rates, or by fees. Sometimes, as did the nobles or the towns during the Middle Ages, an individual acquires the franchise of administering certain ways and taking toll therefor, but the nobles or towns were responsible in the King's courts for negligence in the discharge of the trust, as a town to whom the same trust is delegated by the State is responsible now. Sometimes the construction and maintenance of ways is delegated to a corporation who collects toll, as did the mediæval nobles, for passage upon the way; and these corporations, such as turnpike companies, have been held to be tax collectors standing in the place of the government, and to be subject to all the liabilities which are imposed upon any agent responsible for highways. Bussey

v. Storey, 4 B. & Ad., 109; Commonwealth *v.* Wilkinson, 16 Pick., 175.

In fine, the agency through which the sovereign performs his function as trustee of the people for the construction, maintenance, and protection of their ways is as immaterial as the process by which he raises the revenue by which the work is done. In substance the sovereign is always a public trustee, and, in constitutional governments founded on consent, is accountable to his *cestui* for due performance of his trust. And this doctrine has very recently been solemnly laid down by the Supreme Court of the United States in Atkin *v.* Kansas, 191 U. S., 207.

From first to last, for a thousand years, the law is clear and uniform. The care of the highways is a trust imposed upon the sovereign, which may be delegated, but which cannot be abrogated, and the money needed to execute the trust is a burden upon the people which they must meet by taxes. In the United States the Supreme Court has held in the most emphatic language that the State is the "guardian and trustee for its people" and that "it is one of the functions" of this trustee "to provide public highways for the convenience and comfort of the people." Atkin *v.* Kansas, 191 U. S., 222. Decided November 30, 1903.

I have now reached the point at which I can begin the consideration of the constitutional position of railways, and of the limitations imposed by our fundamental law upon the governments of the United States in their dealings with them.

When railways first came into use their status was uncertain. Sometimes they were built by the State, and sometimes by corporations, but if built by corporations, it seemed clear that they could not be granted the sovereign powers of eminent domain and of collecting rates, if they were common carriers only, or, in other words, if they were a private speculation entered into for individual gain. This question of their public or private status was determined in 1831

in Beekman *v.* The Saratoga & Schenectady R. R., 3 Paige, 45, which arose in New York before Chancellor WALWORTH.

In that litigation the constitutionality of a statute of New York which gave to the corporation the right of eminent domain was disputed because the "defendants are a private corporation, and the road, when made, will be private property; it will not be for public use, but for the private use and emolument of the company, to be used exclusively by its own carriages." 3 Paige, 47, 48. That is to say, the complainant contended that it would be a common carrier, and not affected by a public use, though possibly, like a hotel, subject to police regulation.

"A good boarding house at the Springs is a great accommodation to visitors and invalids; but in order to provide such a house, would it be competent for the legislature to authorize a corporation or an individual to take private property?" *Ibid.*, 48.

In reply the counsel for the railway company made a argument which may well stand as a classic. It convinc the chancellor, it convinced the public; and the princi then advanced has never been shaken, though it seems be disputed by counsel in this cause.

"It is admitted," said he, "that private property may taken without the owner's consent, for turnpike, bridge canal companies. . . . Where is the difference between s companies and this railroad company? Those companies equally with this company authorized to receive all the The only difference is, that this road is not travelled b persons with their own carriages. . . . It is however eq public as a turnpike, as to travelling in a particular way. If the State had made this road, they would have been o to provide the carriages. Yet, in that case, would ar have said that the use was not a public one. . . . Thi pany will not have any power to oppress the pub must charge one uniform price. If it should char

individual an exorbitant price, an action would lie against the company, and it would amount to a misuser of its privileges." And this, he insisted, was so of common right, though the company was not limited in its charges.

"The right of taking tolls is a public franchise, an attribute of sovereignty. This is one of those corporations which are presumed to be founded upon an adequate consideration, received by the government for the franchise granted. It pays a complete equivalent. If the legislature believed that the construction of this railroad would be beneficial to the public, it should have been made by the State, . . . or the requisite power should have been delegated to individuals or a corporation for that purpose. The legislature had a discretion as to the means of effecting the object. The latter is the most common mode now adopted of opening internal communications. . . . But the receipt of tolls cannot vary the question of the public character of this road. Would the Erie Canal have been less a public improvement if no tolls had ever been charged? Or would it be less so now if the tolls should be relinquished?" 3 Paige, pp. 60, 61, 62, 63.

The proposition thus demonstrated, that the railway corporation is not a carrier doing business primarily for private gain, but that it is the agent of the sovereign employed to build and administer a highway for the common welfare, has, since this decision of Chancellor WALWORTH in 1831, been enunciated in numberless cases in both the state and the national courts. In fine, I conceive that no principle in our whole jurisprudence is more solidly established than that the railway is a public work which may be built and operated by the government personally, or which may be built and operated by an agent of the government. But, if the government delegates this function, it still remains responsible as trustee for the people. The supervision of the agent who administers the railway is a part of the police

power, and that power is inherent in sovereignty, and cannot be divested. Munn *v.* Illinois, 94 U. S., 113.

The doctrine, as I have stated it, was laid down a full generation ago by the Supreme Court of the United States in Olcott *v.* The Supervisors of Fond du Lac County, 16 Wall., 678, but it has very recently been affirmed energetically in regard to the Union Pacific.

"The Union Pacific Railroad was a great public undertaking. . . . Congress felt that the public interest required its construction. It sought to interest private capital in the enterprise, and believed that the work could be better done through the instrumentality of a corporation. At the same time it became practically the sponsor for the enterprise by large donations of government credit and public lands. In so doing it was not seeking to aid a purely private enterprise. What it did was in furtherance of the public interests. . . .

"We cannot assent to the contention that the present owner of the property holds it free from obedience to all such legislation. Now, as before the foreclosure and sale, the public interests are to be regarded, and not simply private purposes, wishes or prejudices." Union Pacific R. R. Co. *v.* Mason City R. R. Co., 199 U. S., 169, 170. Decided November 6, 1905.

And in the Sinking Fund cases, 99 U. S., 700, the same Court declared that, "This corporation [the Union Pacific] is a creature of the United States. It is a private corporation created for public purposes, and its property is to a large extent devoted to public uses." 99 U. S., 719.[1]

[1] Probably in making the reservation that the property is to *a large extent* devoted to public uses, and not *altogether* so devoted, the Court had in mind the fact that the Union Pacific received a vast grant of land from the government as a direct bonus to encourage the enterprise, that this land was held for sale for the benefit of stockholders and not as a right of way, and that, accordingly, it might be considered as held for private and not for public use.

Approached thus the reciprocal duties of the State and the railway corporation become clear. The contract between them is regulated by constitutional limitations. The State, as trustee and guardian of the people, is bound to provide the railway as a highway. Sharpless *v.* Mayor of Philadelphia, 21 Penn., 170. It has, however, a choice of means. It may do so itself, or it may do so through an agent, but if it uses an agent, its only justification is that the public will be benefited thereby. Contracts inimical to the common welfare are, therefore, void. For example, no State could bind itself to a private person by a grant which would confer on that person an unlimited power of taxation, in the form of an unlimited power to levy an impost on movement. Such a grant would be void, as I take to have been decided in Owensboro *v.* Owensboro Waterworks Co., 191 U. S., 358; but whether this decision is conclusive or not, the principle is clear.

The State as trustee can only act within the limits of its authority. It cannot take private property and give it to private persons. Therefore if, under the grant of a sovereign power to impose rates upon a highway, a railway, by a tax on movement, takes more than its reasonable compensation from the public, it must hold the balance in trust, because the residuum, above reasonable compensation, must be a confiscation or a trust fund.

It is on this ground, and on this ground alone, that statutes like that of Massachusetts, Revised Laws, C. 14, Sec. 41, can be sustained. That statute requires street railway companies to pay one half of all dividends declared, over a certain amount, into the treasury of the Commonwealth. In other words, it establishes a basis upon which a division of surplus taxes shall be made between the Commonwealth and its agent.

A statute directing a similar division of the earnings of a hotel company would be bad, because it would be confisca-

tion. The hotel is a private enterprise, holding no grant of sovereign power from the government, nor is it in any respect an agent of the State for the performance of its duty as a trustee of the public. The hotel business may possibly be so affected by its relation to the public as to be open to a regulation of rates under the police power, but this regulation of rates would only extend to the protection of the individual against extortion; it would not extend to limiting profits.

This was the distinction drawn by BREWER, J., in Cotting *v.* Kansas City Stock Yards, 183 U. S., 79. He held the stock yard to be in the nature of a monopoly of a necessary accommodation, and therefore subject to police regulation, so far as such regulation might be necessary in order to protect the individual citizen against extortion. The government, however, having given nothing, and the work not being a public work for which the government was responsible as trustee, the State of Kansas could not go on to fix the total compensation to which the corporation was entitled.

The learned counsel for the Northern Pacific errs profoundly when he contends that a railway cannot stand in a fiduciary relation to the public because the public does not share in its losses. The government seldom shares in the losses of any person with whom it contracts for service. For example, it is the duty of the government of the United States to provide for the public safety by building ships of war. In the discharge of this duty it may build warships itself, or it may contract with private persons to build them. If so, the contractor becomes the agent of the government for the execution of this trust, so far as the public is concerned, and the government becomes responsible to the public for the due performance by the agent of his task. The maximum rate, other things being equal, at which the government would be justified in paying such an agent, would be the cost of construction by the government itself; but if,

on this basis, the agent lost money the government would not share in the loss. Nevertheless, the price paid for a battleship may be made to depend, and often does depend, on excellence of performance, the performance to be rewarded by a premium. Of that excellence the government may make itself the judge. Supposing this premium were advanced to the company subject to earning an award in its favor from the government, the company would hold the sum so advanced in trust for the public, until the award had been made.

Similarly a corporation may contract to build a highway, and afterward to operate the same for a reasonable compensation, that compensation to be determined by the legislature subject to the supervision of the courts. Furthermore the rate of reasonable compensation may be variable, depending on the amount of risk, the excellence of performance, and a variety of other circumstances which the tribunal representing the legislature may consider when claims for compensation are advanced by the agent. The whole difficulty arises from the fact that the highway agent is allowed to collect its expenses and compensation by means of an impost, and pay itself in advance. In this it differs from all other private agents. If it collects more than is a reasonable compensation for its services above expenses, it must hold that balance in trust for the public like any tax gatherer, or any other agent possessed of funds of his principal. Thus the task devolves upon the government of fixing what is a reasonable impost to be levied by this agent, and what is a reasonable compensation to be deducted by him from the proceeds of such impost. The government cannot divest itself of this duty if it would. To allow the agent an unlimited power of imposing rates would be as unconstitutional as to convey to it the lands underlying the harbors at its terminals, in order that it might draw an unlimited revenue from them. Furthermore, railways may lawfully be used as tax gath-

erers; they are constantly so used, and are made responsible for the avails of the taxes they collect. Reading R. R. Co. *v.* Pennsylvania, 15 Wall., 274.

Certain fundamental propositions I conceive now to be established. The government, as trustee for the public, is bound to construct the peculiar class of highways called railways for the common use. This trust is imperative and indefeasible; it cannot be contracted away like the prerogative of taxing the individual. Contracts made under this trust are made under a limited authority; only such contracts are valid as conduce to the public welfare. Those which are injurious to the public welfare are void and may be repudiated.

Therefore, contracts relating to railways must be contracts between the government as principal, and the party of the second part as agent, for the government cannot divest itself of its responsibility as principal by any form of contract it can make. Reduced, thus, to its final terms, the contract between American governments and railway corporations must be pretty definite. The government may contract with a corporation to build and administer a railway as a highway for a certain compensation specified in writing, provided that compensation is not inimical to the public welfare; or the government may contract with a corporation to build and administer a railway for a reasonable compensation, that reasonable compensation to be determined by the government itself, under judicial supervision. The government cannot contract to permit the railway an unlimited compensation, for that would be prejudicial to the common welfare.

We next come to the question of the reasonable compensation which may be allowed the agent. Here it is possible to define a minimum compensation under ordinary conditions; it is impossible to define a maximum. I take it to be clear, under the decisions of the Supreme Court, that a railway is

entitled to collect from the public (unless the country is physically unable to pay) a revenue sufficient to cover its operating expenses, taxes, an allowance for depreciation of the plant, fixed charges, and ordinary dividends upon so much capital as stockholders have actually paid into the corporate treasury, of their own funds. Beyond this the railway is not entitled, as of right, to go. If the railway raises a revenue in excess of this amount it holds the balance in trust subject to the order of the government, as supervised by the courts. If, because of risks in the enterprise, excellence of service, or any other sufficient cause, the railway can prove a claim to extra compensation, that claim may be allowed by the tribunal representing the government, but it is a claim to be settled by the adjudication of constituted authority; it is not a claim which the railway can pass upon itself. Conversely, the public may put in any evidence that is relevant, such as an inequality in the assessment of the impost, to establish their right to the appropriation of a part or the whole of this surplus fund, thus held in trust, to the reduction of rates, rather than to any other purpose, such as the improvement or the extension of the highway.

The defendants deny the lawfulness of this method of computing their compensation and advance the propositions which I stated at the beginning of this brief.

They claim that they have a right to collect from the public annually a sum of money sufficient to pay them an income or rental upon a valuation of all the property they hold in trust for the public, appraising this property at the market price of the day. Such a valuation must include not only all additions to and improvements of the line, made by means of appropriations from surplus revenue held in their hands as trustees, after their allowances have been paid, but also the market value of all land held by the railways, whether acquired by private gift, public grant, or purchase with funds drawn from surplus, together with the

unearned increment in value of such lands since the acquisition thereof.

It will be simpler to take up these claims in their inverse order, beginning with the demand for the payment of rental on the unearned increment of land purchased with money contributed by stockholders out of their own funds to the corporate treasury, since this claim is the broadest, and involves the consideration of the title by which railways hold their real estate.

The major premise in all reasoning touching the relation of railways to government is that the government is the guardian and trustee of the people, whose duty it is to provide railways for the public, but who, in making this provision, has a choice of means. The government may act itself, or it may employ an agent. It cannot contract away the ownership of highways so that the highway shall be under private control.

If the government choose the alternative of providing railways through agents, it must do so for reasons which conduce to the public welfare, and not to advance private interests, for to advance private interests by grants of sovereign power, or by gifts of public money, is unconstitutional. The first point, therefore, to consider is the reason which induced American governments to employ agents to build and administer their railways and not to administer them themselves. The reason is found in the history of Pennsylvania. Governments in America had proved themselves competent to build and administer the ordinary highway, but when it came to administering a railway, which is a road together with the mechanism of transportation thereon, popular governments broke down. Hence it appears that the cause which induced private ownership of railways was the difficulty of conducting the transportation business and not the difficulty of providing and holding the right of way.

Under such circumstances it would have been both prac-

ticable and lawful for governments to buy and own the rights of way upon which railways were to be built, or even to build them themselves and lease them to companies, and this policy is often actually pursued with the sanction of the courts. Prince *v.* Crocker, 166 Mass., 347. Every government holds thousands of miles of roadway, as a matter of course. Nothing would have been simpler than for governments to have issued their bonds, paid for the land, and made the interest of the bonds a charge upon the earnings of the line. As governments did not do so the inference is irresistible, that they acted through an agent who bought the lands for public use by the exercise of the right of eminent domain delegated for that express purpose. To have delegated eminent domain for another purpose would have been unconstitutional. Railways, therefore, exercising eminent domain, acquired land for the rights of way, paid therefor with bonds issued as the government might have issued bonds, and the interest on these bonds became a charge upon the earnings of the road, the lands themselves being held in trust for the public. There can be no doubt as to the soundness of this law. In 1842 SHAW, C. J., decided that railways held their land in trust for the public in Worcester *v.* Western R. R., 4 Metc., 564, and this decision has very recently (1906) been approved in Milford Water Co. *v.* Hopkinton, 192 Mass., 491.

Railways do not acquire a fee in their land by proceedings under eminent domain, though they do acquire an estate of corporeal quality because they must have full physical control of the premises. New Mexico *v.* United States Trust Co., 172 U. S., 171. To be precise, I apprehend that they acquire an estate upon condition that it shall be held to the public use as a highway; if that condition be broken the property or the value thereof may be recovered by the original owner or by the State. Proprietors of Locks and Canals *v.* Nashua & Lowell R. R., 104 Mass., 1; In re Flint, 105 Mich.,

289; California & Nevada R. R. Co. *v.* Mecartney, 104 Cal., 616.

The unearned increment in the value of the real estate, thus held by a railway company in trust, is chiefly caused by the operation of the franchise which the company receives as a gift from the public. The defendants put in some very strong evidence to this effect, Portland Evidence, 646, but the fact is notorious. The most ordinary business intelligence on the part of the government, therefore, when chartering a railroad, would have led it to buy the right of way itself, and obtain the increment of value, which it might so easily have done, had it not permitted the railway to buy the land and hold it in trust, on condition that the land should always be devoted to a public use, on the one side, and, on the other, that the public should always pay the interest on the purchase money as well as the taxes on the land itself.

It is elementary law that grants from the public to railways are to be construed favorably to the public, United States *v.* Oregon R. R., 164 U. S., 539, and a contract of the sort contended for by the defendants could never be inferred unless expressed in writing; but even if expressed in an indenture, I apprehend that such a contract would be void as against the public welfare.

The limitations imposed upon an American commonwealth by the public trust, would preclude it from making an irrevocable contract with an agent administering railways, which would subject the public to an indeterminate though perpetually increasing burden which might close the highway. Especially would this be so when no compensation is made, or pretended to be made, for the growing annual charge. Such a contract would pretty clearly be bad. The proposition of the defendants is reduced to an absurdity when the position of such corporations as the New York Central and the Pennsylvania is considered. The unearned increment on the lands held by these companies, whose value, especially

in cities, has been augmented chiefly through the operation of the franchise, is so large that to pay an annual rental of 6 per cent thereon might not improbably raise rates to a level which would stop movement. Under such conditions government ownership would become an immediate necessity.

Lastly, even were doubt on the general question possible, the charters of these defendants provide, in express terms, that they hold their land to the public use.[1]

Thus the construction of the contract for which I contend is not only conformable to the requirements of law, but it is fair to both sides. It is conformable to law, since it would be unlawful for the government, as trustee, to injure its *cestui*, by employing an agent when it might safely act itself. Government might safely buy and hold land; therefore, it would be unlawful for the government to employ an agent to buy and hold land for it, who would charge such a commission as an annual rental of 6 per cent on the unearned increment of that land.

If the lands be bought by the agent and held in trust for the public, the public paying the interest on the investment and taxes, the public stands nearly as well as it would stand if it bought itself, save in regard to the future acquisition of the roads. It would gain, and not lose, as the value of the property gained, by reason of the operation of the franchise which it had given the agent. As the value of the property increased, the credit of the company might, probably improve, and the yearly interest charge, which the public must meet by an impost on movement, would diminish as the company became able to borrow cheaper on its bonds.

[1] Wisconsin Charter of Northern Pacific Ry. Co., Sec. 20:

"All property which the company hereby created is authorized to appropriate, take, possess, hold, or use, by making payment therefor, is hereby declared to be for public use as soon as the company shall so appropriate take, possess, hold or use the same."

The contract is also fair to the roads, for they are under no expense, and are at no trouble, in holding the land. They are not paid for their service as holders of land in trust for the public, which is no inconvenience, and demands no ability. They are paid for the administration of transportation, which is the function wherein the public formerly failed. In order that the corporation may administer transportation, it receives the land free of rent and taxes, since the interest charge on the investment and taxes are paid, holding the same to the use of the public as a highway under penalty of forfeiture. For the service of administration the corporation is compensated partly in salaries which are paid by the public, and partly by dividends upon money invested from their own funds by stockholders in the plant. The size of the dividends allowed by the government must depend on risk, excellence of service, and other considerations. As, however, in any investment in land there is always some chance of depreciation, however remote, this is assumed by the company who buys the legal title. For this risk the company is liberally compensated by the much greater probability of gain, should the government ever acquire the plant under the right of eminent domain, for then the government would have to buy the land at its reasonable market price.

I apprehend that the obscurity pervading this subject comes altogether from the persistent effort of the defendants to confound a valuation of property, as a basis for rates, with a valuation of property as a basis for fixing a price for acquisition by the government through its power of eminent domain.

Very obviously the two valuations depend on different economic conditions, and have little in common except that both valuations must ultimately have for their measure the capacity of the government for personal action.

The valuation for rates is based upon a contract whose point of departure is the power of government, at the incep-

tion of the enterprise, to own a part or the whole of the plant at pleasure. It is a conclusive presumption, that, in the absence of express stipulations to the contrary, where two theories of this contract are possible, that theory must be adopted which will be at least as favorable to the public as would have been personal action by the government. In no other way could the good faith of the government as trustee be maintained. United States *v.* Oregon & California R. R. Co., 164 U. S., 526. The government might well have bought and held the land, therefore it must be presumed that the agent offered equally good terms.

Valuation for condemnation or amicable sale stands on a different ground. In valuation for condemnation it must be assumed that the government is dissatisfied with its contract for agency, and prefers to do the work itself. Such has been, in fact, the case with water companies. The government has been dissatisfied with the water service, has terminated, very generally, the contract of agency, has operated the works itself and, in Massachusetts at least, has improved the works, and saved approximately 25 per cent in water rates. But, in terminating the contract of agency, an entirely new condition is evolved. Both sides start afresh. Works are in existence to which the government has no title. It can buy them, or it can duplicate them, Charles River Bridge *v.* Warren Bridge, 11 Peters, 420; but if it buys them it must pay at least as much for them as it would cost to build and put in operation other works which would be measurably as effective as those which are for sale. It is here that the corporation has the advantage of the unearned increment of its land. Nor can the public complain at having to pay this increment, since it had the choice at the outset to buy the land, or fix terms on which it might acquire the land, and did not do so. It preferred to remain altogether out of the business, put the whole plant in trust, leaving the legal title in the agent, and take the chances of

a rise or fall in the price of the land, should the public in future have to take possession. Probably, also, this would prove, on the average, no bad business arrangement, since the power of duplication always remains, which, in the majority of cases, would bring the selling price, in the case of acquisition, within resonable limits.

I submit that, upon this theory of the law, railways cannot value the unearned increment of any land, no matter how acquired, as a basis for assessing a rental against the public, to be collected by means of rates.

It next remains to be determined what categories of land they are justified in putting on their schedules at all; and first comes the category of lands acquired by the appropriation of surplus after the just allowances of railways as agents have been paid. This category I maintain is plainly unlawful, but before entering on the subject I must define what I contend to be a *just allowance.* The rate of profit permitted by government to a railway corporation must be sufficient to attract capital, else the railway could not be built by an agent. Government must pay what capital is worth, like other people. In the case of the Union Pacific, it paid high. But part of this compensation may be paid by a bonus, such as a grant of land for sale, and this would go to decrease risks, and proportionately to decrease the rate of dividends allowable. I use the Great Northern land grant as an illustration. Suppose that an allowance of 7 per cent dividends, plus a land grant worth $12,000,000, had been enough to cause capital to invest in the Great Northern, as it doubtless would have been, since the investment in the Great Northern was attended with little or no risk, as the projectors well knew; any revenue above the amount needed to pay operation expenses, taxes, an allowance for depreciation of the plant, and fixed charges and dividends at 7 per cent, would be surplus, which the road would hold as trustee, awaiting the order of the government as to application thereof. Failing direc-

tions as to application, if the road, in its capacity as trustee, invested this surplus in permanent improvements or extensions of the plant, those extensions or improvements would become public property, subject to any claim the road might establish before the government tribunal, for extra compensation as reward for high efficiency in the public service.

If this proposition be denied by the defendant the denial is tantamount to a claim to confiscate or to embezzle private property, for it is the claim of a collector of taxes to appropriate to his own use the balance of taxes remaining in his hands after the cost of collection and his own compensation have been paid. Twist this proposition how you will it always comes back to this: Either the railway is an agent, in which case it is accountable for all sums it may collect from the public in excess of expenses and due compensation; or it is a sovereign, when it is not accountable at all. Only these defendants are not content to be constitutional sovereigns; they pretend to the prerogative of despotic and arbitrary sovereigns, since they claim a right to take the property of the public without compensation and apply it to their private use, as William the Conqueror took the property of the peasants, whose villages he destroyed, to make the New Forest. I need not say that such a claim transcends the constitutional power of American governments to countenance.

Of course, I do not deny that if the defendants, being authorized to divide 7 per cent, divide only 5 and turn 2 per cent into capital, the land so acquired would be acquired by a contribution of private funds. What I do maintain is that, when the full amount of reasonable costs and dividends has been taken from earnings, all investments made in the plant with surplus beyond that amount are made on public account, and in such investments the railway can only share to the extent to which its claim to extra compensation for extra service may be allowed by government.

The second category of land which the defendants claim to place upon their schedules, and which I contend that they have no right to enter thereon, is land acquired by public grant.

As BLACK, C. J., held long ago, in Sharpless *v.* Mayor of Philadelphia, 21 Penn., 170, "The making of a railroad is a public duty . . . it follows that such a work may be made partly by the State, and partly by a corporation, and the people may be taxed for a share of it, as rightfully as for the whole." Accordingly, governments have always aided railway construction, either by the issue of bonds or by the grant of lands, or by both, as circumstances might require, but such contributions have been a fixed liability, and made to secure a public benefit. Thus the United States granted both the Union Pacific and the Northern Pacific tracts of land to sell, and the State of Minnesota granted the Great Northern a tract worth $12,000,000. The grant of the right of way is different. That grant is made with the intention of cheapening the cost of construction, and thereby lightening the burden to the public, and such is the manifest intent of the grant to the Northern Pacific, Acts of 1864, C. 217, Sec. 2, as it is also the manifest intention of the Act of 1875, C. 152, under which the Great Northern acquired most of the right of way for its Pacific Extension. But even were it not the manifest intention of these acts that the defendants should hold land granted them to the uses I have indicated, if such an intention can possibly be ascribed to these acts, it must be so ascribed, since such grants are always construed as favorably as possible to the public: "Only that which is granted in clear and express terms passes by a grant of property, franchises or privileges in which the government or the public has an interest," Coosaw Mining Co. *v.* South Carolina, 144 U. S., 562, and the public can have a keener interest in few things than in not being charged a rental upon a right of way which it has given to a corporation, and whose market value

appreciates by leaps and bounds in the manner thus described by Mr. Hayden, the Great Northern expert:

"I will just say in regard to North Dakota, we built into a country that is developing and has developed very rapidly since the lines were put in there. . . . Since that time that country has settled up very fast and towns have sprung up along our lines, and the lands have appreciated, and the right of way would cost a great deal more to-day to purchase than we paid for it." Portland Evidence, 645, 646.

Furthermore, it would be unconstitutional for Congress or a State legislature to make such a grant, as it would be a violation of the public trust. Grants of public property can be made to private persons only to serve the public welfare, but a grant of a right of way on which the public must forever pay a rental would leave the public in precisely the same position as if the corporation had bought the land with its own money. Nothing would have been gained by the grant. The grant of public property would, therefore, have been made purely for the emolument of private persons, and, were such a grant proved, the only effect would be to avoid the grant, and cause the right of way to revert again to the government, as the flats under the harbor of Chicago reverted to the State of Illinois after the State had granted them to the Illinois Central Railroad. Illinois Central R. R. *v.* Illinois, 146 U. S., 387.

Lastly, I come to land acquired by railways from private persons, nominally as a gift, but really on condition that certain services be performed, as the right of way through Spokane was acquired by the Great Northern from citizens of Spokane on condition that the Great Northern would concede terminal rates to the city.

It is admitted that the Great Northern has not performed the condition, and yet it retains the land, and this land appears upon the schedules as part of the land on which the public must pay a rental at its present market value. This claim

is of surpassing effrontery, even for these defendants. One of the excuses made by the Great Northern for the non-performance of the condition was that the right of way so granted had been of no value as a right of way, though it was the land designated by Mr. Hill as the land he wished to obtain for that purpose; and that therefore it had not been used for railway purposes, and another right of way had been bought. Spokane Evidence, vol. 1, pp. 148, 168, 169.

It is elementary law that a railway can only hold land for the purposes for which it is chartered, and that if it holds land for other purposes, as, for example, ordinary business purposes, it holds the land wrongfully. Such land, if acquired by eminent domain, is held wrongfully against the original owner, and *a fortiori*, land which has been conveyed for a particular purpose on a condition which has been broken, reverts to the grantor, since the consideration has failed. The railway, therefore, even if it has not lost its title altogether, is liable for mesne profits. The Supreme Court of Massachusetts has explained this principle very lucidly:

"In respect to lands taken by railroad corporations, although the discretion of the directors is unlimited, as to the mode and extent of the use or occupation, for the purposes for which the corporation was created, yet it is definitely limited by those purposes. Any uses of the land confessedly for other purposes, or not apparently for purposes permitted by its charter, are not protected by its authority. For such uses the owner may have his redress by any appropriate action." The redress in that case was a judgment for mesne profits to be reckoned as "the full, clear annual value of the land." Proprietors of Locks and Canals *v.* Nashua & Lowell R. R., 104 Mass., 11, 12.

Far from the Great Northern having a claim against the public for rental for this property, therefore, the grantors of the Spokane right of way have a claim for the mesne profits of these lands during fifteen years, against the Great Northern.

Touching the purely legal aspect of the questions propounded by the Commission, I might, perhaps, here close my argument; but I conceive that no examination of these questions can be thorough which does not extend to an analysis of certain modern economic phenomena which are the cause whereof the propositions of the defendants relating to valuation are the effects.

Among the various defences made to this petition, not one is an honest effort to reach an equitable agreement between the corporations and the public for the compensation of the defendants as agents of the government administering highways. The reason is not far to seek.

The modern railway corporation has a double function. It is at once the builder and maintainer of a highway, like a turnpike company, and a carrier enjoying a monopoly of transportation on the road it has built. As the successor of the turnpike company as a highway builder, it claims sovereign privileges from the government, but it makes its money from the transportation business, and therefore its profits largely depend on its power to fix prices to meet its financial interests.

As I have shown by a long line of precedents, extending from the Ship Money to the Dred Scott decision, the tendency of courts of justice, in conflicts between vested interests and the public, is somewhat to favor the vested interests, especially in the earlier stages of these controversies. Possibly this tendency may be essential to the stability of society, possibly it may be an instinct rooted in lawyers by their training; at all events, the phenomenon is incontestable, and the judge-made law which has been evolved by the rise of modern railways is no exception to the general rule.

Just seventy-six years ago Chancellor WALWORTH held, in Beekman *v.* The Saratoga R. R., that railways succeeded to the claims which the courts have recognized when made by turnpike companies. That is to say, he held them to be

agents entrusted with a public work by government, and therefore entitled to exercise such sovereign powers as the State would have exercised had the State acted personally. This was logical and consistent. But when it came to limiting profits, the courts inclined to give the railway companies all the latitude enjoyed by common-law carriers, who held no monopoly in their dealings with the public. Such a judicial policy followed in the line of precedent, since the capital vested in railways is the largest mass of consolidated capital in the world, and the courts are lenient toward all dominant power.

In my first brief, pp. 22–33, I have analyzed these decisions in their historical sequence.[1] They were doubtless made by judges from the purest motives and with the object of protecting those whom they felt society was bound to protect, precisely as MARSHALL thought himself defending the oppressed in the Dartmouth College case. So much may be readily conceded, but the practical effect of those decisions has been to lodge an absolute and arbitrary power of taxation in the hands of private persons; and now, for nearly a whole generation, the people, through their legislatures, have

[1] Before the statute of 1887 the courts were inclined to permit the roads to discriminate, practically at pleasure, both between persons and localities. After the statute, while somewhat more cautious as to personal discriminations, because the roads themselves found rebating disastrous, the courts upheld local discriminations which were profitable, overruling the Interstate Commerce Commission. The following are some of the chief cases favoring discrimination referred to in the text: Fitchburg R. R. *v.* Gage, 12 Gray, 393; Concord & Portsmouth R. R. *v.* Forsaith, 59 N. H., 122; C. C. C. & I. Ry. *v.* Closser, 126 Ind., 348; Lough *v* Outerbridge, 143 N. Y., 271; Ex parte Benson, 18 S. C., 38, which is a very extreme decision. The leading cases on this phase of the statute are Interstate Commerce Commission *v.* Baltimore & Ohio R. R., 43 Fed. Rep., 37, for Jackson's well known exposition of the meaning of the statute in substance following the Massachusetts rule, see page 50; affirmed, 145 U. S., 263; Interstate Commerce Commission *v.* Alabama Midland Ry., 168 U. S., 144; East Tennessee, Virginia and Georgia Ry. *v.* Interstate Commerce Commission, 181 U. S., 1; Interstate Commerce Commission *v.* Louisville & Nashville R. R., 190 U. S., 273.

been seeking to abridge this power and enforce the public trust. It is the latest of these statutes designed to enforce this trust which your Honors are now about to construe.

Hitherto, because of the inertia of the judiciary, the railway system of the United States has been left very much to be moulded by the varying social conditions which have prevailed in divers sections of this country. Finally, these differing conditions have caused railway administration to split into two sharply defined schools. One of these schools I shall call the monopolistic, the other the public-service school. The monopolistic system of administration is based upon the imposition of the monopolistic price, and this may be defined as scientific discrimination against the weak. The public-service system is certainly an attempt to treat all men equally. These two systems cannot permanently coexist; one must eventually absorb the other, as I shall show.

As representatives of these two schools, Mr. Hill's combination is the most perfect type of monopoly; the Pennsylvania, the most perfect type of public service. And I most respectfully submit that it is only by comparing the methods and the effects upon society, of these two rival schools of administration that the scope of this controversy can be measured. The problems presented are complex, but the crux of the conflict lies in the power to charge the monopolistic price; and it is only when this axiom is borne in mind that the defences made in this cause are comprehensible. The one paramount purpose of these defendants is to invent some ground upon which the imposition of the monopolistic price shall be made to appear reasonable. The claim to charge the public a rental on the unearned increment of a right of way granted by government, is only the most flagrant of these devices.

Were I to perform exhaustively the task I have outlined, I should begin with a history of the organization and the

subsequent development of the Pennsylvania Railroad. This is impossible, even were it permissible, since such a work would require a stout volume. All that I can attempt is to refer by way of illustration to certain salient characteristics of the Pennsylvania, which are of common knowledge.

And, at the outset, I must premise that the policy of the Pennsylvania has not always been uniform. I speak here only of general tendencies which have become steadily more accentuated with the lapse of time. Also great and deplorable abuses have occasionally existed in the Pennsylvania management. For my purpose these are immaterial. Abuses exist in every human institution. The essential is that when abuses among Pennsylvania officials have been exposed they have been admitted and corrected. Under monopolistic systems similar abuses have been defended and continued.

I shall consider the Pennsylvania policy under three heads: 1st, the collection of revenue; 2d, the expenditure of revenue; 3d, the raising of funds for improvements. Organized as a State highway, the Pennsylvania has always retained many of the characteristics of its origin. The fundamental principle of its being is that it has recognized its responsibility as a governmental agent, and has made dividends subordinate to public service. As the government is bound to assess its taxation equally, so the Pennsylvania has endeavored to assess its rates equally. All citizens are supposed to receive an equal service for an equal payment. That discriminations have been made does not impugn the rule. When those discriminations have been proved, they have been adjusted. In fact, discriminations have been the inconsiderable exception, and equality has been the rule, and this intelligent appreciation of the common welfare has made the interior of Pennsylvania the wonder of the world. Furthermore, by equality of assessment the railway company has raised

enormous sums of money without injustice and without burdening the community.

Passing now to the matter of expenditure, no corporation, possibly, in the whole world has spent so lavishly on construction, on equipment, or on accommodations for the public, and much of this lavish expenditure has been drawn from surplus. Moreover, this expenditure of the public money by the Pennsylvania, in its capacity as trustee, has been as honestly and as wisely made as it has been equally and equitably provided for. Its staff has been well paid, has been loyal, and has been kept at the highest point of efficiency. Nothing has been spared to ensure punctuality, efficiency, safety, and comfort.

The residue of its earnings, after the public service has been performed, has been divided among stockholders. Dividends and salaries have been liberal, but they have been no more than a fair compensation to the agent. The policy has not been to divide on cumulative capitalization, which is the characteristic of the monopoly. I proceed to illustrate: For the vast works which the Pennsylvania has undertaken in recent years, surplus earnings have been insufficient. Additional funds had to be obtained, and the problem which the Pennsylvania direction sought to solve was how to raise the maximum sum of money with the least issue of obligations, in order that the company might have the fullest benefit, and the public might carry the lightest burden. The terms on which issues of stock have been made to cover late improvements, may be studied as a lesson in honest and able financiering, and the result has been that during 1907 the Pennsylvania, almost alone among the railways of the United States, has responded to all the demands made upon it, without undue effort, and without having divided a dollar of bonus among its stockholders. On the contrary, far from giving a bonus, the company made the stockholders subscribe for their new issues of stock at a higher price than the stock was worth.

Any stockholder would have been richer who had sold his rights when they were issued, and bought his stock after issue in the open market.

The monopolistic system of railway administration is the converse of the public-service system, because in the monopolistic system the public service is but a vehicle by which to obtain private profit. Its vital principle is to exact the highest price and render the least return. The three most striking examples of the potency of monopolistic processes in the United States are the Standard Oil, the United States Steel, and Mr. Hill's combination in the Northwest. All the three have employed the same methods, but they have differed in this: the Standard Oil and United States Steel are private enterprises which have succeeded by energy and thrift; Mr. Hill alone has obtained and employed sovereign powers for the purpose of wholesale confiscation. Coming into a poor and sparsely settled country many years ago, Mr. Hill has consistently used a national highway to enrich certain foreign speculators, precisely as a Roman proconsul might have plundered a conquered province. Also he has ignored public responsibilities. While the Pennsylvania was spending hundreds of millions in providing for a future expansion which intelligent men foresaw, Mr. Hill was engaged in dividing his surplus among his stockholders by dividends of watered and undervalued stock, deliberately enfeebling his railways, until last winter the country tributary to them starved amidst the snow. Also the discontent among Mr. Hill's staff is notorious. His niggardly management is hated alike by the public and the employees. On the other hand, the profits to the syndicate which Mr. Hill organized have been dazzling.

The secret of Mr. Hill's success has lain in his ability to maintain and impose the monopolistic price, which is the issue in this suit, and to defend which he has brought forward his scheme of valuation. Now the monopolistic price

has thus been defined by Professor Ely in his book on "Monopolies and Trusts," and Professor Ely's definitions have been adopted by the Supreme Court of the United States in National Cotton Oil Co. *v.* Texas, 197 U. S., 129.

On page 99 Professor Ely says: "The gains of the monopolist may be regarded as a function of two interdependent variables . . . the number of sales and the profit on each. What the monopolist wants, therefore, is to get that combination of number and profit which will give him the maximum net returns. . . .

"Monopoly, then, as we have seen, means variation in price, not only from time to time and from place to place, but even from individual to individual. *Class price*, however, is a better term than individual price, if we have reference to the conditions of modern industrial society; for monopoly price to-day, in the more important cases, means class price," p. 114.

Examined by this test, Mr. Hill's policy shows genius. To thoroughly succeed, the first business of the monopolist is to suppress competition, so that he may be able to extract from his victim all that that victim can pay. His next is to graduate his demands to conform to the limit of the victim's endurance. Mr. Hill first acquired a monopoly in the Northwest by the operations which I have described in my first brief. He then set himself to establish his scale of prices, his problem being to keep all his equipment moving at the highest velocity for the highest price. To do so he graduated his charges to conform to the resisting power of every community and every class in the community. He has often boasted that his average rates are low. Mr. Hill has made low rates to secure business, if he needed that business and if it could be had on no better terms; perhaps no railroad in the country has made lower. But if the rate be for a necessary of life to be sold to a population under servitude to his monopoly, his charge will be the limit of what the purchaser can pay.

Many years ago Mr. Clough, the vice-president of the Great Northern and Mr. Hill's confidential adviser, explained, in the first suit between these parties, the process by which the company reached the monopoly price.

I have thus quoted from his testimony on page 123 of my first brief:

"*Q.* So you carry shingles and lumber from Seattle to St. Paul for 50 cents a hundred, to keep these people from starvation, . . . and you charge $4.75 a ton to haul wheat from Spokane over to Puget Sound?

"*A.* That is a fair rate, as compared with other rates on the system.

"*Q.* Well, are you in doubt as to whether you make money on that basis or not?

"*A.* No, we are not making too much.

. . . . . .

"*Q.* In other words, then, you have to have so much money?

"*A.* We have to have so much money, yes, sir, and we have to get it from our patrons; there is nobody that gives it to us.

"*Q.* And therefore you go for the people that you think have got in a place where they can't help themselves?

"*A.* We try to arrange our rates as far as possible so that the business will move."

This testimony of Mr. Clough's illuminates Professor Ely's definition of the monopoly price. Mr. Clough described how he obtained the maximum function of his variables, the variable of price and the variable of sales. The substance of success has lain in making the price just low enough to permit the community to buy all that the monopoly has to sell; that is to say, in this instance, to keep its rolling stock constantly moving. This implies, of course, discrimination carried out scientifically as between individuals,

classes, and localities, and this is the system which Mr. Hill has practised, as far as practicable, and herein has lain his success.

And that his success has been complete, the subjoined analysis of his report will show. His success has been so complete as to be embarrassing. One of his chief preoccupations has been to devise means of converting the surplus taxes he has thus collected from the people to his own use, without divulging the amount of his exactions. Sometimes when his surplus has grown unwieldy he has distributed it in huge blocks, as when he distributed the certificates for the ore lands which he had bought with surplus, or as when, at an earlier day when his ideas were smaller, he issued $10,000,000 of bonds for one tenth of their face value. But ordinarily he has preferred to invest his surplus in additions to his lines, thus giving him the power to make a cumulative increment of capital out of public money, and collect an income on this increment. The advantage of this method of financiering is palpable. Every dollar of public money thus confiscated is forthwith protected as being a vested interest, and on that vested interest Mr. Hill may divide 7 per cent forever. Furthermore, he may collect thereon as much additional tax as the public can pay, and he is free to invest that surplus also in subsidiary monopolies.

Evidently such a system as this cannot permanently co-exist with the public-service system; the pecuniary advantage it has over its rival is relatively too great. If the monopolistic system be permitted to prevail, it must absorb public-service systems as the Great Northern absorbed the Burlington, since the profits to those who own stock in public-service systems may be doubled thereby.

These facts, as well as the deductions to which I have alluded as following therefrom, appear fully in the subjoined analysis of the official financial statements made by Mr. Hill to his stockholders. If opportunity permitted, a similar

of corporate property in good faith, as a basis upon which to compute a reasonable compensation for the services of the corporations he represents as agents administering highways, but as a method of defending the nefarious exactions imposed upon the public by the maintenance of the monopolistic system of administration.

That, in pursuance of this duty, the national government has created the tribunal to which your Honors belong, and that upon its creation the duty devolved upon your Honors of enforcing the public trust.

That Mr. Hill became long ago one of the agents whom governments has permitted most extensively to administer the national highways, since Mr. Hill has, admittedly, had the substantially uncontrolled management of several of the most important railways of the Union.

That in the administration of these railways, as president of a railway corporation, and therefore as agent for government, Mr. Hill was bound to administer them equally for all, and so as to conduce to the public welfare.

That, in order to enable him to perform this duty, Mr. Hill's corporations received great grants of public property, as well as grants of the sovereign powers of taxation and of eminent domain, and that it was Mr. Hill's duty to see to it that these concessions of public property and of sovereignty were used for the common good.

That, in especial, Mr. Hill, as president of the Great Northern, was entrusted with the power of levying an impost upon traffic passing upon his highways for the purpose of enabling him, first, to defray the cost of administration from the proceeds thereof; second, to take from said proceeds reasonable compensation for the services, as agents, of the corporations he represented; and, thirdly, to hold any surplus income which might remain in his hands from the avails of these imposts, after the above deductions had been made, to the public use as trustee for the public.

Such, I submit, is the law upon this subject as it has been expounded by our highest tribunals, both judicial and legislative. I proceed now to lay before you an exposition of the manner in which Mr. Hill has, in fact, discharged this trust. I do so, among other reasons, in order that I may show that Mr. Hill is not now advancing his theories of the valuation

1906, inclusive, as capital, and the valuation which the Great Northern Railway Company put upon its property, after twenty-seven years of administration, in 1906; the difference between the two is the increase in value on the investment.

3. The methods by which this increase has developed.

4. That at least sixty-eight millions of dollars ($68,000,000) of income or earnings have been converted into capital in the Manitoba system and its successor, the Great Northern Railway Company.

5. That forty-four millions of dollars ($44,000,000) of water have been injected into the capital.

6. That, together, the earnings and water so capitalized exceed one hundred and twelve millions of dollars ($112,000,000) or 35 per cent of the entire capital shown in the balance sheet of June 30, 1906.

7. And, finally, that the directors of this railway system, a trustee for the public, have given to their shareholders immediate advantages affecting the taxation of the public (and exclusive of dividends) to an amount exceeding four hundred and sixteen millions of dollars ($416,000,000) together with ore lands the ultimate value of which will add more than one billion of dollars to this sum.

This I shall show by a series of balance sheets.

Minneapolis & Pacific Railroad Company

The Congress of the United States, by Act of March 3, 1857, to encourage railroad construction, granted to the territory of Minnesota six sections of land per mile, and under the Act of March 3, 1865, this grant was increased to ten sections per mile. The legislature of the territory of Minnesota chartered, March 22, 1857, the Minneapolis & Pacific Railroad Company. The legislature granted to the company all the lands granted to the territory by Con-

gress in the acts above referred to for the purpose of aiding the construction of a railroad by the prescribed route. This company having failed to pay interest on its bonds under the deed of trust to the State, the State foreclosed the trust deed and became the purchaser of the property on June 23, 1860. On March 8, 1861, the charter was restored to the old company on conditions which were not complied with and again said company was dispossessed.

St. Paul & Pacific Railroad Company

March 10, 1862, the State granted all rights, etc., of the Minneapolis & Pacific Railroad Company, acquired by the governor by this purchase, to the St. Paul & Pacific Railroad Company.

Pursuant to an act of the legislature February 1, 1864, the St. Paul & Pacific Railroad Company was divided into two companies: that portion commencing at St. Paul and terminating at Breckenridge and a branch line to Sauk Rapids taking the name of the First Division of the St. Paul & Pacific Railroad Company, the remaining portion (not then commenced) still having the old name of the St. Paul & Pacific Railroad Company. In 1871 the last-named company, in which were vested all the franchises, grants, etc., from St. Cloud to St. Vincent and to Brainerd, leased its property for ninety-nine years to the First Division, by which the construction was undertaken. To provide for the construction of this road an issue of bonds was made in 1871 and handed over to a firm in Amsterdam, Holland, for sale, and from this source funds were supplied until late in 1872. At that time the necessary supply of money was stopped. Return for Fiscal Year, December 31, 1872, F. C. vol. 17, p. 381.

The reason follows:—

The suit of J. S. Kennedy & Co. and others against the St. Paul & Pacific and Northern Pacific Railroads in the

United States Circuit Court for the District of Minnesota resulted in having Jesse P. Farley of Dubuque appointed receiver for what is known as the St. Paul & Pacific Railroad, comprising the extension from Watab to Brainerd and from St. Cloud to St. Vincent, a total distance of 400 miles. He completed the uncompleted portion of the road and thereby secured the land grant. He was authorized to borrow funds to complete the same. F. C. 17, 220, 381, 1873.

The receiver completed 112 miles of road at a cost of $9000 per mile, as against $30,000 per mile expended by the company on the other portion of the road. F. C. 29, 19.

In 1877 negotiations which had long been pending were concluded at Amsterdam and London, whereby a majority of each of the five classes of the mortgage bonds covering the main and branch lines of the St. Paul & Pacific Railroad Company had been purchased by a new organization of Canada and Minnesota capitalists, thus transferring to them the controlling interest of the St. Paul & Pacific Railroad Company, including the First Division. "New stock is to be issued 60 per cent of which will be held by Messrs. Kittson & Hill of St. Paul and the remainder by the Canadians while new bonds are to be issued to the Canadian parties for an amount sufficient to cover the cost of purchase and the cost of completing the St. Vincent extension." F. C. 25, 424, November 3, 1877.

This is the first public appearance in the affairs of this road of Mr. James J. Hill, who afterward became general manager and president of the reorganized road.

The statement herein made, namely, that new bonds were to be issued to the Canadian parties, "For an amount sufficient to cover the cost of purchase, also the cost of construction of the uncompleted road," shows the amount of money which Mr. Hill and his Minnesota associates originally put into the enterprise to be none whatever; also the source from which real money was obtained for purchase and con-

struction, viz., from Canadian capitalists represented by Mr. George Stephen of Montreal and Mr. Donald A. Smith of Winnipeg, and that the money was to come from bonds.

The Canadian capitalists offered prices for the outstanding bonds of the St. Paul & Pacific, varying from 11 per cent and 13¼ per cent for the St. Vincent Extension bonds to 70 per cent for the First Division Branch Line bonds, interest included, and 3.3 per cent for $500,000 par value of Red River & Manitoba stock. F. C. 25, 408, 1877, and F. C. 27, 68, 1878.

They secured the bulk of the bonds outstanding. F. C. 31, 21.

"Messrs. Hill and Rice representing the new owners of the St. Paul & Pacific Railroad report the transfer of the bond holding interest from the Dutch holders to Canada and Minnesota parties completed. The new proprietors have obtained a majority of the bonds on favorable terms which will place them in possession of the road . . . after foreclosure . . . at a cost of not more than $10,000 in gold per mile." F. C. 26, 342.

Foreclosure, was effected in June, 1879.

The bonds to the amount of $486,000 upon 10 miles of road from St. Paul to St. Anthony and 80 miles to Sauk Rapids were not foreclosed.

The sale of the branch line from St. Paul to Watab to J. S. Barnes, of New York, for the bondholders brought $200,000. F. C. 28, 495.

The main line, St. Anthony to Morris, 150 miles, $250,000. F. C. 28, 580.

The extension $1,600,000.

Several suits were brought by non-assenting bondholders, but unsuccessfully, to reopen the litigation, and the receiver instituted suit for his portion of the proceeds. F. C. 28, 616

St. Paul, Minneapolis & Manitoba Railway Company

The St. Paul, Minneapolis & Manitoba Railway was organized May 23, 1879, by the selection of these directors:—

George Stephen, Montreal (president);
Donald A. Smith, Winnipeg;
J. S. O. Barnes, New York;
Norman W. Kittson;
H. R. Bigelow;
R. B. Galusha, and
James J. Hill (general manager), St. Paul. F. C. 28, 555.

This company acquired the St. Paul & Pacific Railroad, the First Division of the St. Paul & Pacific Railroad, and the Red River & Manitoba Railroad, — 565 miles — completed railway, running from St. Paul and Minneapolis to the boundary line between the United States and Canada, and there connected by the Canadian Pacific with Winnipeg, including railway from Minneapolis by the way of St. Cloud to Alexandria.

In order to acquire the completed and equipped railway and 2,000,000 acres of the best land in Minnesota, and worth, land alone, $12,000,000, the Canadian interest took care of the issue of first-mortgage 7 per cent gold land-grant bonds of $8,000,000, *infra*.

The cost of all of the property — 2,000,000 acres of the best land in Minnesota; 565 miles of railway, fully equipped and in operation — did not exceed $12,000 per mile, $6,780,000. How this amount was raised, independent of any stock issue, next appears.

In a circular issued by J. S. Kennedy & Company, of New York, F. C. 29, 226, issued for the purpose of sale of these $8,000,000 of bonds, it is said that the St. Paul, Minneapolis & Manitoba Railway was organized out of the St. Paul & Pacific, First Division of the St. Paul & Pacific and Red River & Manitoba Railroad Companies,—565 miles of completed

railway. . . . The mortgage under which the above bonds are issued covers the entire property of the company including the 2,000,000 acres of land at the rate of $12,000 per mile completed road. The proceeds of sales of land are especially devoted to a sinking fund to be applied by the trustees to the purchase of the bonds at or under 105 per cent. There is no prior indebtedness upon the property except old mortgages for $486,000, $120,000 upon 10 miles of railway (from St. Paul to St. Anthony) maturing in 2 years and one $366,000 on 80 miles due in 1893, both of which the company is prepared to pay off. The total amount of bonds provided to be issued is $8,000,000, of which $6,780,000 is now to be issued. The entire issue has been sold by the company and a limited amount is now offered to the public at 104 per cent.

The official reports of the company show the company to have acquired 565 miles of railway complete, equipped, 2,000,000 acres of land for the $6,780,000, or $12,000 per mile, exclusive of the land, *supra*. This land, including that acquired with the Minneapolis & St. Cloud grant, returned to this company, through the sinking funds, to which the proceeds of land sales were assigned, to June 30, 1906, $13,068,887, Annual Reports, Sinking Fund Commissioners, and there remained to be sold, beyond the reduction in acreage through adjustment with the government, 182,000 acres, Annual Report, Great Northern, 1906, 33, 37, 38, the value of which it is impossible to determine.

From the foreclosure sale of the railroad the clerk of the Ramsay district court, Minnesota, paid the following dividends to holders of St. Paul & Pacific bonds and overdue coupons after paying receivers' debentures: —

On the bonds of the $1,200,000 mortgage of 1862, $796.49 per $1000 bond, being 59.256 per cent; on bonds of the $2,800,000 First Division Mortgage of 1865 10.7 per cent, being $163.69 per $1000 bond; on bonds of the $6,000,000

First Division Mortgage of 1868 19.774 per cent, being $285.27 per $1000 bond. F. C. 29, 147.

A second issue of bonds — second-mortgage bonds, — $8,000,000, was made in October, 1879, for the purpose of extending the railway and of completing any portions of the road which might then be under construction. F. C. 29, 513.

At the organization of the St. Paul, Minneapolis & Manitoba Railway Company there was issued $15,000,000 of stock which, if the agreement entered into between the St. Paul and Canadian interests was carried out, — and there is no reason to doubt that it was (since Mr. Hill and his associates have controlled and now control it), — Mr. Hill and his St. Paul associates received 60 per cent and the control, and the Canadian interests, who advanced the money which paid for the railroad and land, 40 per cent secured by first mortgage on land and railway, *supra*.

All of the first balance sheet issued by the new Manitoba Company, June 30, 1880, published in the Financial Chronicle, vol. 31, p. 281, follows: —

INCOMPLETE BALANCE SHEET, JUNE 30, 1880

First year of operation of the St. Paul, Minneapolis & Manitoba Railway Company.

Assets

Cash in bank	$653,181
Cash for bond interest	293,108
Cash in sinking fund	419,354
Due from roads and agents	196,458
Union Depot stock	20,000
Stock and material on hand	570,990
	$2,153,091

Cost of railway, equipment and lands	$31,297,028	
Bonds redeemed	161,100	
		$31,135,928
(The balance sheet as published, F. C. 31, 281, contains an apparent omission of items or else profit or loss of $550,955 as the footing is carried down)		$33,839,974

Liabilities

Unpaid bills		$1,100,707
Unpaid coupon and accrued interest		421,999
Funded debt.		
1st mortgage bonds	$8,000,000	
Retired	161,100	
	$7,838,900	
2d mortgage bonds	8,000,000	
St. Paul & Pacific bonds	486,000	
	$16,324,900	
Capital stock	15,000,000	
		$31,324,900
(An apparent omission here necessary to a balance is an item of profit and loss, of $992,367)		$33,839,974

In the last analysis the above balance sheet expresses the inducement to form the syndicate.

Public contributions:

1. The franchise from the State of Minnesota.
2. The right of way under Act of Congress of 1875, c. 152, sec. 1: 100 feet on each side of the central line of said road, also land for station buildings, side tracks, workshops, etc., not to

exceed 20 acres for each station to the extent of one station for each 10 miles of railroad (1026.88 miles, and from the State of Minnesota 139.88 miles, acquired by Pacific Extension. Exhibit filed with Commission April 29, 1907).

3. Land grants: 2,580,606.23 acres after adjustment with the government, Great Northern Report, 1906, 37, 38, from the sales of which bonds of the par value of $11,925,400 have been redeemed, Great Northern Report, 1906, 33, plus the premium paid from sinking funds thereon, $1,143,487, Sinking Fund Commissioners' Reports, 1880–1906, — a total of $13,068,887, leaving still unsold in 1906, 182,034.54 acres after adjustment, Great Northern Report, 1906, 37, 38.

Against all this land the syndicate advanced on a 7 per cent gold first mortgage $8,000,000
Every dollar of which has been repaid from the proceeds of the land sales.

With the sale of $6,780,000 of the bonds under the above mortgage the syndicate acquired legal title to the land and to 565 miles of railway, fully equipped, with which to develop and market the land the only encumbrance thereon being mortgages to the amount, since paid . $486,000

The reward:

On acquiring title to the lands and railway, the syndicate issued to themselves 150,000 shares of stock, for which no money went into the treasury of the new corporation, but which is added, at its full par value, to the cost of railway lands and equipment to balance its issue $15,000,000

The money at risk:

Money being needed to extend the railway, a second mortgage, 6 per cent, was created upon the railway, but not upon the lands . .	$8,000,000
This $8,000,000 was the only money really risked in the venture, the only money not secured by public grant. Probably the corporation received little thereon; the first market quotation was 80. An examination of succeeding balance sheets fails to reveal how much if any of the avails of the second-mortgage bond issue was ever permanently invested in the railway. All of the first-mortgage and a part of the second-mortgage bonds have been redeemed.	
This, then, was the method of arriving at the cost of railway lands and equipment	$31,486,000
against this total cash risked some portion of	$8,000,000
and the basis of the present cost of the Manitoba system	$140,981,778

Great Northern Report, 1906, 33.

The total unprotected, uncovered cash payment by the syndicate was but $8,000,000, the second mortgage. The first issue of land-grant first-mortgage bonds was $6,780,000, that sum having been issued for the railway lands and equipment, and if the corporation received par value for its $8,000,000 first-mortgage bonds there remained $1,220,000 of that issue (and exclusive of the second mortgage) available for other purposes. Ninety-one miles of new road were put in operation the first year ending with the above balance sheet, F. C. 31, 281, approximating in cost $12,000 per mile, $1,092,000, and paid for, doubtless, out of second-mortgage bonds.

The first year's operation yielded a surplus $555,790, *infra*, so that the cash in bank exclusive of sinking fund is amply accounted for in support of the assertion that the first issue of $15,000,000 of stock was water.

It is admitted by the syndicate's bankers that the doubly secured cash cost to the syndicate of this entire property, lands, railway, and equipment was but $6,780,000. F. C. 29, 226, *supra*.

The Supreme Court of Minnesota set the actual cost of the railway, lands, etc., at $3,600,000 only and yet $16,000,000 in bonds and $15,000,000 stock were issued:

"Of the lines of railroad here in question 561 miles were built for and owned by other railroad companies prior to the foreclosure sales of 1879. At one of these sales the promoters of the St. Paul, Minneapolis & Manitoba Railway bid off a part of the property. These properties, the franchise connected with the same and a large land grant, earned and to be earned, were bid off for the aggregate sum of $3,600,000, subject only to a prior lien of $486,000. The promoters transferred to the new company the part bid in by them, and the properties were immediately bonded by the new company for $16,000,000, and it issued to the promoters its stock to the amount of $15,000,000." Steenerson *v.* Great Northern Railway, 69 Minnesota, 320.

The slimness of this first balance sheet demonstrates the fact that the first issue of $15,000,000 of stock by the St. Paul, Minneapolis & Manitoba Railway Company, and which gave to Mr. Hill and his associates the control of the present vast system, was water. Absolutely no consideration in money moved therefor to the St. Paul, Minneapolis & Manitoba corporation. The foreclosed road, 565 miles fully equipped, with 2,000,000 acres of land, was purchased with $8,000,000 first-mortgage bonds; the extensions to date of balance sheet were financed by an issue of $8,000,000 second-mortgage bonds.

No money was paid to the corporation for this first issue of stock, $15,000,000. It was water and the cost of the road inflated to balance its issue.

It will be remembered that after the foreclosure sales of 1879 the Manitoba Company issued to its promoters $15,000,000 of its stock. Some time afterward it issued $5,000,000 more, which was sold for cash at par. Steenerson *v.* Great Northern Railway, 69 Minnesota, 400.

There had been chartered in Minnesota the Minneapolis & Northwestern (narrow gauge) road and the stockholders had subscribed upon its $150,000 of stock 10 per cent ($15,000) paid in. They had contracted for a quantity of iron, and incurred other liabilities. The Manitoba road for $10,500, on July 15, 1880, swallowed this narrow-gauge road, refunding 7 per cent of the 10 per cent that the stockholders had paid in; further, the Manitoba road agreed to construct the Union Depot at Minneapolis and build 100 miles of standard-gauge road northwesterly from Minneapolis for a bonus of $1000 per mile, and there the responsibility of the city was to end. F. C. 31, 96.

In his annual report for the year ending June 30, 1880, President Stephen outlines the policy of road which, persisted in, is, in the application of earnings, one secret of the enormous value put upon the Manitoba and Great Northern properties at the present time.

"There have been expended on improvements of roadbed, purchase of right-of-way, fencing, water stations, etc., $340,676 and on new equipment $497,021 which sums have been provided for from funds reserved for that purpose at organization of the company, while more than ordinary expenditures for maintenance and repairs have been charged to operating expenses.

"The real estate purchased and permanent improvements represented by the sum of $357,185 in the general statement comprises the land acquired by the company for a Union

Depot at Minneapolis and ground for additional yard room and workshops at St. Paul, new general office building and large freight warehouses at St. Paul and other property which adds largely to the assets of the company." F. C. 31, 281.

Here is the nucleus of the great terminals at Minneapolis and St. Paul whose valuation in 1907 Mr. Hayden estimates to be $13,945,925 and $7,114,547, respectively. Portland Exhibits, 1485.

It is to be borne in mind, in connection with the cost of this Union Depot at Minneapolis and the extension of the narrow-gauge railroad at standard gauge, that the Manitoba company received from the city of Minneapolis $100,000, *supra.*

No further issue of stock for money was authorized in 1880 or 1881, the extensions being financed, as was the purchase of the St. Paul & Pacific, by bonds exclusively.

In 1881 the Manitoba Company acquired the charter of the Minneapolis & St. Cloud Railroad Company to which attached a land grant of ten sections per mile. Under this acquisition the Manitoba Company added to its holdings of lands earned from the state 425,660 acres, on which there had been realized to June 30, 1906, $1,286,753.90 leaving 21,220 acres of the St. Cloud land grant (and 160,814 acres of the original Minneapolis & Pacific grant) still unsold. Annual Report, 1906, 37, 38, *supra.*

The company built the 200 miles of Dakota Extension in 1881 through the issue of bonds for $2,400,000, $12,000 per mile on 200 miles of completed and equipped railway. Annual Report, 1881, F. C. 33, 254.

No stock, bonds only, and $12,000 per mile.

These roads were laid with iron rails and wooden bridges which were later replaced with steel rails and steel bridges, but the steel rails and steel bridges when they appeared were paid for from earnings. F. C. 35, 264. The annual report

for 1882, F. C. 35, 264, shows 1058 miles in operation, an increase of 209 miles in 1881 and 192 miles in 1882, paid for with bonds.

The first dividend on the $15,000,000 of stock, 3½ per cent, was paid August 1, 1882, and the original stock had a market value after three years of operation of 140.

Under date of June 8, 1882, but not appearing in balance sheet, new stock to the amount of $5,000,000 was offered to stockholders at par, to provide funds for continued development of the property, including certain extensions and branches already made or in contemplation and for other purposes. The stock will thus be increased to $20,000,000. F. C. 34, 655.

This was the first issue of stock for which the company received par value in money. The stock had at this time, as a stock on a 7 per cent dividend basis, a market value of $140 per share, and this issue was worth, at the market quotation, $7,000,000, a bonus of $2,000,000 to the stockholders.

I wish to insist that was the first issue of undervalued stock, as well as the first stock issued for money.

In the annual report of June 30, 1882, President Stephen admits:—

"The replacement of iron with steel rails, improvement of roadbed, renewal of bridges, etc., has been charged to operating expenses and no charge has been made for transportation of the company's material for construction of new lines or the renewal or repair of old ones." F. C. 35, 264, *supra.*

Under date of April 13, 1883, the company gave this notice to stockholders:—

"The Board of Directors for the purpose in effect of reimbursing to and dividing among the stockholders the cost and value to the extent of $9,000,000 of large and valuable properties and lines of railway recently acquired by the

company; and not covered by its existing mortgages, and of extensive improvements and additions to its other properties, conferred upon its stockholders of record, May 1, 1883, the privilege of acquiring consolidated mortgage 6 per cent 50-year gold bonds of the company *of a new issue*, to the amount of 50 per cent of their holdings, *at the price of 10 per cent of the par value thereof*." F. C. 36, 427.

Nine million dollars of water was here mixed with the bonds in addition to $15,000,000 of water already in the capital stock, and the company is to-day distributing $1,590,000 annually thereon. A "privilege conferred."

Mr. James J. Hill became president of the Manitoba Company in 1883.

In his annual report of 1883 President Hill, commenting on this issue of $10,000,000 of bonds at 10 cents on the dollar by a railroad already paying 7 per cent dividends upon $15,000,000 of watered stock and $5,000,000 cash stock, says: —

"The Board of Directors, on April 12 last, authorized stockholders to purchase the new consolidated mortgage bonds of the company to the amount of 50 per cent of their holdings at 10 per cent of their par value which privilege the stockholders have availed themselves of. This action was deemed by your Board wise and for the best interests of the company in view of the fact that new properties and lines of railroad had been acquired, *the value* of which had been added to the property and *fairly belonged to the stockholders and ought properly to be represented in the fixed charges of the company*." F. C. 37, 320.

"During the past year an agreement was made between this company and the Northern Pacific Road by which some of the new east and west lines in process of construction by this company were exchanged for north and south lines that had been built by the Northern Pacific. Such an adjustment of existing differences was also had as will prevent

disastrous competition between the respective lines." F. C. 37, 320.

It is plain that Mr. Hill's ultimate idea of monopoly had not at this time developed. His present intention evidently was to provide a railroad from the south to the north which should cross the transcontinental lines at the points of connection, and that sufficient business, which would well repay the stockholders and the bondholders for their outlay, could be so obtained.

President Hill, in advance of his annual report of this year, admits: —

"The Manitoba Road is now operating 1350 miles of line, $1,700,000 *have been expended upon its equipment from the earnings of the road without the issue of bonds.*" F. C. 37, 152.

President Hill's admission is timely, for the financial statements do not show such expenditures either in gross earnings or revenue or income accounts.

The future policy of the Manitoba road adopted by the Great Northern system is clearly outlined in President Hill's annual report of 1884: —

"In view of the large expenditures that require to be made from time to time for replacement of iron with steel, purchase of new equipment and permanent improvements, it has been deemed wise by the directors to set aside a fund to especially provide for these extraordinary expenditures when they occur and it is their intention in the future to set apart therein each year such sums as the earnings of the road will justify until this is ample for any contingency." F. C. 39, 324.

Twenty-four million dollars, or 46 per cent of the capitalization of $51,368,000, in 1884 was water.

In 1885, in the annual report, President Hill says:—

"Last year attention was called to the necessity of a fund for permanent improvements, replacement of iron with steel, new equipment and other extraordinary expenses; with a

view of carrying this into effect the directors unanimously resolved in October, 1884, to reduce the quarterly dividends from 2 per cent to 1½ per cent." F. C. 41, 306.

The company then had unexpended in this fund (which at that time was designated a reserve fund) $651,000.

This reduction in dividend rate still gave the stockholders $1,200,000, or 24 per cent annually on $5,000,000 of cash capital and 6 per cent on the entire capital, including the $15,000,000 of water.

The annual report of 1887 contains this:—

"In the face of these heavy and continued reductions in rates the capacity of your property for producing sufficient revenues not only for payment of its capital charges and operating expenses but also for steady and constant betterments of its physical state by the substitution of steel for iron rails, the additions of shop, yard and terminal facilities on an ample scale and approved plans, the elimination of curves from the lines, the lowering of grades, securing of new and approved equipment and the like has remained unimpaired." F. C. 45, 511.

All this increase in earning capacity was through conversion of earnings.

This 1887 balance sheet shows among the assets Minneapolis transfer stock, $7000; Minneapolis transfer bonds, $63,000; Union Depot stock, $70,000; Minneapolis Union Railway stock, $750,000: a total of $890,000, for the acquirement of which no stock or bonds were issued, — no appropriation made therefor, — they simply appear in the balance sheet acquired with earnings.

The following circular was issued to stockholders by the directors March 21, 1887: —

"This company having obtained authority from the Congress of the United States to extend its lines through the Indian Reservation in Northern Montana and Dakota and to continue the same to the Great Falls of the Missouri

River, and the necessary legislation having also been obtained from the legislature of Montana, your directors have determined to proceed at once with the construction of the line from the present terminus in Dakota to Great Falls, a distance of about 540 miles. . . . At Great Falls it will connect with the Montana Central Railway. . . . For the completion of that portion in Dakota means have already been provided, and for the purpose of providing the necessary funds to complete and equip that portion between Fort Buford and Great Falls a distance of about 400 miles, your directors have decided to issue $7,000,000 4 per cent bonds . . . to be a first mortgage on the Montana Division with a specified amount of equipment to be marked and numbered and a schedule of same to be attached to the mortgage and delivered to the trustees thereunder. This will make the amount of the mortgage on the road and equipment about $17,500 per mile, but, as the rapid settlement and development of the country will probably necessitate the building of branches and extensions at an early date, the mortgage will be made to cover a total issue of $25,000,000 of bonds with a proviso that for any future branches or extensions none shall be issued except against road completed and equipped for an amount not exceeding the actual cost thereof and in any event not exceeding $25,000 per mile on the average." . . . F. C. 44, 402.

The mortgage above referred to was offered to stockholders at 80 flat, payable in instalments, which was probably a fair market price for it. No stock was issued for this extension. Whatever was necessary in the way of capital beyond 80 per cent of $17,500 per mile for 540 miles and an ultimate average of $25,000, on what was at that time the most expensive portion to build, came from earnings.

In 1887 the Manitoba road acquired a controlling interest in the stock of the Lake Superior & Southwestern Railroad. No stock or bonds were issued for this purpose and

the property could have been acquired from bonds and earnings only. This marked the nucleus of the immense holdings of land at the head of Lake Superior which afterward appeared as an asset of the Eastern Railway of Minnesota. F. C. 45, 511.

The balance sheet of 1887 had shown a valuation upon the Manitoba property of $65,903,047, of which $20,000,000 was stock ($15,000,000 water, $5,000,000 cash paid in), $46,298,977 bonds ($9,000,000 water, $37,290,977 cash paid in) less $3,009,000 of land-grant sales, and plus $3,400,000 invested in other property.

Mr. Hill had not in 1887 conceived the idea that the moneys received from sales of public grants should be added to the capitalization of the system; and the amount of land-grant bonds redeemed through sales of public lands is deducted from the valuation of the property. Balance sheet, Annual Report, 1887, F. C. 45, 512, appended hereto:—

BALANCE SHEET, JUNE 30, 1887

Assets

Cost of railway, lands, and equipment (inflated to meet issues of stock and bonds)		$65,903,047
Minneapolis Union Depot stock	$70,000	
Minneapolis Transfer Co. stock and bonds	70,000	
Minneapolis Union Railway stock	750,000	
		890,000
Other properties and securities		2,592,158
Material, money due, etc.		2,615,020
Cash on hand		2,169,800
		$74,170,025
Less grant bonds redeemed		3,009,000
		$71,161,025

Contra

Stock ($15,000,000 water)	$20,000,000
Bonds ($9,000,000 water) less $3,009,000 redeemed by land sales	43,289,977
Sinking fund cash	583,888
Interest, taxes, etc.	279,338
Payable	3,608,988
Fund improvement and renewals	1,023,945
Profit balance	2,374,889
	$71,161,025

On both sides of this sheet the valuation is reduced by the amount realized in sales of the granted lands. We therefore find 63.1 per cent of the capital is cash paid in, 36.9 per cent of the capital claimed in the stocks and bonds is water.

President Hill, in an official circular issued to stockholders in 1888 said: —

"We now propose to complete the line of the Wilmar & Sioux Falls Railway about 150 miles and the Duluth, Watertown & Pacific Railway about 73 miles in southwestern Minnesota and Dakota, the control of which has been secured by your company. . . . It is also necessary to build about 60 miles of new local branches. To complete this work it is necessary to provide from $5,000,000 to $6,000,000 and your directors feel that the method adopted for raising the amount should be such as to *confer a benefit* on the stockholders. They have therefore resolved to create a mortgage to secure $8,000,000 5 per cent bonds to be secured by a deposit of the following stocks and bonds: —

Eastern Railway of Minnesota stock	$5,000,000
St. Paul, Minneapolis & Manitoba Con. Mtg. bonds	750,000
Northern Steamship Company stock	1,500,000
Montana Central Railway bonds	500,000
D. W. & P. bonds	1,375,000
W. & S. F. bonds	2,625,000
	$11,750,000

The $8,000,000 of collateral bonds above referred to were issued to stockholders at 75 per cent. F. C. 46, 228.

A 5 per cent bond of the Manitoba system paying 6 per cent dividends, these bonds were worth their par value in the market. Mr. Hill calls the $2,000,000 thus presented to his stockholders, a "benefit conferred." I have adopted his expression in a tabulation of these "benefits."

The source from which the Manitoba Company obtained the above securities, together with $5,000,000 of Montana Central Railway stock later shown, is not so plain. No stock had been issued since 1883, and this development was four years later, and no bond issues were made for the specific purpose of acquiring these stocks. They were earnings or water.

The view that the Minnesota courts took of the situation is better expressed in their own language: —

"At the time of the lease of its road by the Manitoba Company, in 1890, a large amount of miscellaneous property was sold and transferred by said Manitoba Company to said Great Northern Company. Said properties consisted of the following items of the agreed value set opposite each as follows:—

Bonds

Willmar & Sioux Falls Ry.	$2,625,000
Duluth, Watertown & Pacific Ry.	1,375,000
Montana Central Ry.	500,000
St. P., M. & M. Ry.	100
St. P., M. & M. Ry., Montana Extension	6,000
Minnesota Transfer Ry.	109,000
Todd County	30,000
Town of Hutchinson	12,000
Town of Breckenridge	4,300
County of Pipestone	30,000
Town of Minnesota Falls	2,000
Town of Sandness	2,000
	$4,695,400

Stocks

Eastern Ry. of Minnesota	$5,000,000
Montana Central Ry.	5,000,000
Willmar & Sioux Falls Ry.	1,500,000
Duluth, Watertown & Pacific Ry.	730,000
Northern Steamship Co.	1,500,000
Minneapolis Union Ry.	500,000
St. Paul Union Depot	70,000
Minneapolis Transfer Co.	7,000
St. P., M. & Manitoba Ry	5,600
Sand Coulee Coal Co.	250,000
Climax Coal Co.	149,000
St. Paul Foundry Co.	75,000
Ft. Benton Bridge Co.	11,600
Lake Superior Terminal Ry.	16,700
	$14,814,900

Other Properties

Land Contracts	$621,771
St. Anthony's Elevator	39,382
Hotel Lafayette	207,075
Minnesota Beach Lands	75,202
Pine Lands, Mille Lacs County	53,503
Devil's Lake Town site	23,361
Sundry Town sites	5,000
St. Paul, Minneapolis & Manitoba Ry. bonds	750,000
Land grant, St. Cloud & Hinckley	553,525
(cents omitted)	$2,328,823

"Said properties so transferred were of the aggregate value of $21,839,123 and were paid for by the Great Northern Company by its stock then issued to the amount of $20,000,000 in the manner following, as shown by the reports to the commissioners in evidence. The properties so transferred, as aforesaid, were subject to a lien of $9,250,000. The stockholders of the Manitoba Company paid to the Great Northern

Company $10,000,000 in cash, and transferred to it said properties as aforesaid. The Great Northern Company assumed and paid said lien of $9,250,000 and thereupon issued to said stockholders of the Manitoba Company $20,000,000 of Great Northern stock, each stockholder of the Manitoba Company being given a share of the stock of the Great Northern for each share that he held in the Manitoba.

"For the purposes of this case (a case involving rates) said $20,000,000 of great Northern Ry. Co. stock represents only $10,000,000 paid in. The rest is water. These other properties above enumerated not only represent these $10,000,000 but, as we have seen, they must also represent over $11,000,000 more of the proceeds of these $84,000,000 bonds issued by the Manitoba Company with which proceeds these properties were originally acquired and yet the interest on all these bonds is charged up against the earnings of the Great Northern Ry. Co.'s road. Thus, if the position of the court below is correct, the stockholders of the Manitoba Company have succeeded in taking out over $11,000,000 of its capital, on which the road must still earn an income." Steenerson *v.* Great Northern Ry., 69 Minnesota, 400, 401, 402.

The balance sheet of 1889, on the strength of which showing the initial issue of Great Northern stock was made, showed a valuation in the Manitoba system of $91,958,188 made up as follows: —

Assets

Cost of railway, lands, etc., including equipment	$78,522,595
Other properties and securities	1,537,261
Stocks owned (par value $15,053,100)	4,168,167
Bonds owned (par value $5,448,725)	5,424,225
Due the company	789,375
Material on hand	280,519
Cash balance	1,236,045
	$91,958,188

Contra

Capital stock	$20,000,000
Bonds outstanding	60,985,000
Sales of land	3,598,514
Money due and accrued interest	3,575,520
Fund improvements and renewals	1,310,830
Profit balance	2,488,324
	$91,958,188

F. C. 49, 657.

Division of Assets

Cost of railway, lands, etc., including equipment:		
Inflation of cost to cover issue of watered stock 1879–80	$15,000,000	
Inflation of cost to cover issue of bonds in 1883	9,000,000	
Total water in capital	$24,000,000	
Money put into capital including land sales	54,522,595	
		$78,522,595
Cost of other properties		1,537,261
Cost of stocks owned (par value $15,033,100)	$4,168,167	
Costs of bonds owned (par value $5,448,725)	5,424,225	
		9,592,392
Due the company		789,375
Material on hand		280,519
Cash on hand		1,236,045
		$91,958,188

Division of Liabilities

Stock paid for in cash	$5,000,000
Bonds for which cash was paid in	51,985,000
Land sales to redeem bonds	3,598,514
Vouchers and interest accrued	3,575,520
Carried forward	$64,159,034

Brought forward		$64,159,034
Fund for improvements and renewals	$1,310,830	
Profit balance	2,488,324	
Representing earnings put into system which might have been paid out in dividends earnings capitalized		3,799,154
		$67,958,188
Water in stock, 1879		15,000,000
Water in bonds, 1883		9,000,000
		$91,958,188

Dividends, $1,200,000, 24 per cent on cash stock paid in.

Cash capital in system, including land sales . . . . . $60,583,517 — 68.5 per cent

Water and earnings converted to capital . . . . . $27,799,154 — 31.5 per cent

Admitted Annual Surplus after Dividends

	Improvements	Admitted Surplus	Total Surplus
1880		$555,790	$555,790
1881		732,466	732,466
1882		985,085	985,085
1883		1,656,631	1,656,631
1884	$381,545	610,677	992,222
1885		1,052,321	1,052,321
1886		454,380	454,380
1887	600,000	257,591	857,591
1888	750,000	598,925	1,348,925
1889		130,736	130,736
1890		513,560	513,560
	$1,731,545	$7,548,162	$9,279,707

Annual Reports, 1880–90.

In addition to the above it is admitted that in 1883 $1,700,000 had been converted from earnings to equipment, *supra*. The additions to cost of property for equipment shown in balance sheets of 1888, 1889, and 1890, aggregating $2,121,156, doubtless came from earnings also, and these items would increase the above admitted surplus to $13,100,863.

The ownership of securities of the cost value of $11,129,653 and of the par value $22,000,000, led to the formation of a new company in which they could be capitalized at par; another "benefit conferred" on stockholders.

President Hill said of these securities in his annual report of 1889: —

"The financial statement shows over $22,000,000 of other property, stock in proprietary companies and bonds held by this company the value and income from which is increasing and belongs to the shareholders. It would be unwise to separate any of these properties from this company." F. C. 49, 656.

At this period the surplus earnings which had been converted into capital and held by the corporation in common were distributed in severalty to the stockholders.

In November, 1889, the plan was formulated and given out in an official circular to stockholders of the Manitoba: —

"A large part of the railway extensions made under the auspices of this company has been made by corporations, the stock and bonds of which have been, to a large extent, acquired for your benefit, and this company now holds such securities and other property to an amount of over $22,000,000 par value, of which $11,750,000 have been deposited as security for $8,000,000 collateral trust bonds. Your Directors were of opinion that the value of these securities could be most readily applied to the benefit of all stockholders by transferring them to a new corporation which should undertake the charge of all railways now managed or controlled by this [Manitoba] Company, together with the

necessary extensions thereof, guaranteeing regular and permanent dividends and in the organization of which you should have the preference. . . .

"Preferred stock will be issued at par but the stockholders of this company will only be required to pay $50 per share in cash, the other $50 being paid by the transfer to the new company of the assets already mentioned, but subject to the lien of the Collateral Trust mortgage for $8,000,000.

"Bonds secured by the Collateral Trust mortgage of the company for $8,000,000 will be accepted on account of subscription to the preferred stock as the equivalent of cash.

"The Great Northern Railway Company will pay off, and cancel the $8,000,000 Collateral Trust mortgage bonds of the Manitoba Company." F. C. 49, 435.

The stocks and bonds of proprietary companies were, it will be observed, in the possession of the Manitoba Company before the collateral bonds were issued; the bonds did not pay for these proprietary companies' stocks, earnings acquired them.

The Great Northern Railway Company on and after February 1, 1890, has conducted the business of the St. Paul, Minneapolis & Manitoba Railway, paying interest on bonds, taxes, and assessments on the property, taking the revenue, out of it, paying rental, 6 per cent on $20,000,000 of capital stock, on a lease of 999 years.

An official circular from President Hill of the Great Northern to stockholders, March 22, 1892, contains the following: —

"Since this company on February 1, 1890, leased the lines of the Manitoba Railway it has operated them with results entirely satisfactory to all interests. Prior to the execution of the lease to this company it was contemplated that the lines of the Manitoba should be extended to Puget Sound and provision was made in the lease for the construction of this extension and the issuance of securities by the lessor (St. Paul, Minneapolis & Manitoba Company) to

cover the cost. Pursuant to the terms of this lease the lessor authorized the creation of its Pacific Extension mortgage to secure an issue of bonds amount of £6,000,000 . . . and your company has entered into a contract with the Manitoba Railway Company to construct the extension for the proceeds of said bonds. . . . Your directors consider it proper that such methods shall be adopted to provide the necessary funds to complete the work as will secure to you a further interest in the property. They have, therefore, resolved to create a mortgage to secure $15,000,000 bonds and as collateral security therefor to deposit with the trustee of said mortgage £3,000,000 of the Pacific Extension bonds of the Manitoba Company. The bonds are to run 10 years from September, 1892. . . . This company reserves the right to redeem at any time after September 1, 1893. The opportunity is now offered stockholders to subscribe pro rata at 72½ per cent." F. C. 54, 525.

The Manitoba Company issued no stock after 1882. Except for such earnings as may have been put back as capital, the £3,000,000 Pacific Extension bonds issued by the Manitoba Company paid for the Pacific Extension, completed in January, 1893, and open for traffic in June of that year.

In the last analysis of the cost of this Pacific Extension, the 818 miles completed for the $15,000,000 then issued, the cost per mile, completed, equipped, and open to traffic, was $18,300 per mile, $36,600 per mile if the entire issue was used. The £3,000,000, amounting to less than $15,000,000 in exchange, was all of the Pacific Extension bonds that were issued for a number of years; and it was said by the president, in his report, that "the completion of the Pacific Extension practically completes the work of construction for the company," and without an issue of stock.

In 1892 President Hill of the Great Northern Railway Company calls attention to the bonded debt of the Manitoba and the very low rate of bonded debt and fixed charges

per mile of road. There was at that time in the Manitoba system 2921.17 miles of road bonded for $18,365 per mile and $6846 capital stock per mile, a total of $25,211 per mile. F. C. 55, 1037. Extract the $9,000,000 of water from the bonds, the bonded debt is $16,900 per mile; extract the $15,000,000 water from stock, and the stock is $1711 per mile, a total capitalization, bonds and stock, of $18,611 per mile.

In October, 1898, occurred the purchase of the $20,000,000 of Manitoba, a 6 per cent stock, with $25,000,000 stock of the Great Northern Railway Company. F. C. 67, 1003.

In 1901 the Manitoba road voted to the Great Northern Company improvement bonds $5,000,000 to reimburse the Great Northern for earnings converted to capital account through additions and improvements to the Manitoba system, and paid for out of earnings which might have been paid out in dividends. F. C. 72, 580.

Cost of railway, land, and equipment of St. Paul, Minneapolis & Manitoba Railway Company June 30, 1906, $140,981,778. Great Northern Annual Report, p. 33.

Mileage June 30, 1906, Great Northern Report, 1906, 35 exclusive of side tracks, 3932 miles.

Cost per mile on $116,981,778 of money paid in capital and capitalized earnings $29,700 per mile.

The above does not include cost of stock of the Manitoba corporation and did include in the item of net "cost of securities owned by Great Northern Railway Company" June 30, 1906, $70,658,727, of which the following is a part: —

Cost of stock of the St. Paul, Minneapolis & Manitoba acquired at the exchange into Great Northern stock in 1899 at 125 per cent . . .	$24,566,250
Less par value of the 196,530 shares then acquired	19,653,000
Net cost of securities above par	$4,913,250

Annual Reports Great Northern, 1899, F. C. 69, 958, and 1906, 33.

Great Northern Railway

The Great Northern Railway Company began operations February 1, 1890.

Directors: James J. Hill, St. Paul, president; W. P. Clough, St. Paul; Samuel Hill, Minneapolis; Sir George Stephen, Sir Donald A. Smith, Montreal; George Bliss, New York; M. D. Grover and E. Sawyer, St. Paul; J. K. Tod, New York.

The Great Northern Company controlled a valuable lease of the Manitoba property in return for 6 per cent annual dividends upon $20,000,000 of stock, the payment of interest upon the bonds, taxes, and assessments.

It had two million dollars ($2,000,000) in cash after it paid off the St. Paul, Minneapolis & Manitoba, $8,000,000 collateral trust bonds out of $10,000,000 paid, and started in life with securities of a par value of $22,000,000, *supra*, which it listed as having cost $19,250,000. F. C. 51, 683. Of the issue of $20,000,000 capital stock, therefore, in the inception of the Great Northern system, $10,000,000 was money and $10,000,000 represented "accumulations" of the Manitoba system.

Here was an exchange of securities of doubtful value paid for by the Manitoba system from income for Great Northern stock whose value was for future demonstration.

The Great Northern preferred stock was quoted in February, 1890, at 71.

It was in 1891 that President Hill, in his annual report, thus spoke of the extension of the road to the Pacific coast: —

"An extremely favorable pass over the main range of the Rocky Mountains has been found for this line, permitting a maximum grade to the eastern approach of 52.8 feet per mile, no tunnel being necessary. The descent of the western grade will also be favorable, both as regards grade and curvature. When this extension has been completed your com-

pany will have a continuous rail line from Lake Superior, St. Paul, and Minneapolis to the Pacific Coast, shorter than any existing transcontinental railway and with lower grades and less curvature. Its cost and capitalization will also be much less than those of any other line to the coast." F. C. 51, 682.

Official circular from the president to the stockholders of March 22, 1892: —

"Your Directors consider it proper that methods shall be adopted to provide the necessary funds to complete the work as will secure to you a further interest in the property. They have, therefore, resolved to create a mortgage to secure $15,000,000 of bonds and as collateral they have deposited with the trustee of said mortgage £3,000,000 Pacific Extension bonds of the Manitoba Company. These bonds are to run ten years from September 1, 1892, bear interest at four per cent. The company reserves the right to redeem them at any time after September 1, 1893. The opportunity is now offered the stockholders to subscribe pro rata at 72½," F. C. 54, 525, *supra*, — an undervaluation of bonds.

Apparently the Pacific Extension was paid for without the aid of stock, bonds and the surplus earnings of the Manitoba system paid the cost.

In May, 1893, there was an issue of Great Northern stock. The issue is thus referred to in the annual report of 1893: —

"The completion of the Pacific Extension during the last year makes the length of this system approach 5,000 miles of railway with important steamer connections. . . . The necessity of additions to the equipment of the railways and to the fleet of steamships controlled by this company, and of dock and other terminal facilities, was recognized. To secure the funds needed for these and other purposes your Directors decided the best plan would be to increase the stock by $5,000,000 at par." F. C. 57, 898.

The above was an issue of undervalued stock. The stock

was issued to shareholders at par. The market value of the stock was 140.

This issue of undervalued stock put $2,000,000 in the pockets of stockholders in addition to the annual 5 per cent dividend. A "benefit conferred."

In the fiscal year ending June 30, 1894, the Great Northern Railway Company showed a decrease from the preceding year in revenue exceeding $2,000,000, and had to avail itself of the surplus income of proprietary companies, the Manitoba system having failed by $908,170 to meet its rental charges, in order to pay the usual dividend of 5 per cent. Even then there was a deficiency, after this dividend, of $104,153. F. C. 59, 1144.

The idea of monopoly had not, in 1894, fully developed, for President Hill, in his annual report for that year, stated:—

"With the completion of its line to the Pacific Coast the company has no further extensions in view." F. C. 59, 1144.

In 1895 the company earned the dividend, and admitted a surplus of $131,671, and this after the payment of $900,000 of the rental of the Manitoba road on $15,000,000 of watered stock, — $540,000 on $9,000,000 of water in bonds, and $500,000 on $10,000,000 of stock exchanged for the securities purchased from the Manitoba Company, $1,940,000 then annually, now $2,552,000 annually, on "investments" of this character.

In 1897 there was expended from earnings in permanent improvements on track alone $900,000. F. C. 65, 927.

In 1898 Great Northern stock went to 180.

The company gave notice that it would redeem the entire issue of $15,000,000 collateral trust 4 per cent bonds, and the only issue of bonds ever made by the Great Northern Company (and for which its treasury had, at 72½ per cent, received $10,875,000), by an issue of 7 per cent stock. The issue was $25,000,000, and stockholders paid $60 per share. The balance of $40, to bring the issue to par, was credited

to each stockholder who released his equity in Seattle & Montana stock, which had been paid for with earnings. F. C. 66, 1189.

This stock issue not only exchanged a 4 per cent bond, exclusively held by stockholders and those under them, for a 7 per cent stock, but the capital in the treasury of the Great Northern Company derived no benefit therefrom.

At 180 the $25,000,000 stock had a market value of $45,000,000, or $30,000,000 more than par value of the bonds it retired. The issue substituted for a fixed charge of $600,000 per annum on $15,000,000 4 per cent bonds a dividend charge of $1,750,000 on $25,000,000 of stock.

Here was a stock dividend par value of $10,000,000, a 40 per cent dividend in 6 per cent stock on $25,000,000 of stock then outstanding.

In October, 1898, occurred the exchange of the $20,000,000 of Manitoba stock for $25,000,000 par value of Great Northern stock. F. C. 67, 1003. Great Northern stock had an average market value in the month of issue of 192, and a share and one quarter for every share of Manitoba represented a market value of $240 per share for Manitoba stock.

For the $15,000,000 par of watered stock which the Manitoba stockholders voted themselves in 1879, and on which, continuously since 1882, dividends of at least 6 per cent had been paid, they now received Great Northern stock having a market value of $36,000,000.

The capital stock of the Great Northern Railway Company was now, in 1898, $75,000,000.

Cash paid in for stock:

First issue, 1890	$10,000,000	
Second issue, 1890	5,000,000	
Third issue, 1898	15,000,000	
Annual Reports, 1890, 1894, 1899.		
Second issue Manitoba, 1882, *supra*	5,000,000	
		$35,000,000

Earnings in stock:		
First issue, 1890.		
Accretions of Manitoba Co. . .		10,000,000
Water in stock:		
Third issue, 1898	$10,000,000	
Fourth issue, 1898. Water in Manitoba stock, exchanged for Great Northern	15,000,000	
Fourth issue, 1898. Premium on St. Paul, Minneapolis & Manitoba stock	5,000,000	
		30,000,000
		$75,000,000

Cash capital, 46.67 per cent.

Water and earnings, 53.33 per cent.

Dividends, 6 per cent on full issue; 12.8 per cent on capital paid in.

In April, 1899, $15,000,000 of Great Northern stock was offered stockholders at par. 1899 Report, 5, 6.

It had a market value of 190, thus securing for the corporation treasury $15,000,000 on stock which had a market value of $28,500,000. On the basis of the right to purchase one share of new stock for every five then held, this issue was, in effect, a privilege or "benefit conferred" of $38 per share.

The cash capital paid in was now $50,000,000 and the dividend paid in 1900 $6,408,777. Annual Report, 1900, F. C. 71, 659. 7 per cent on $90,000,000 of stock out, and 12.8 per cent on $50,000,000 cash paid in.

From the revenue of the Manitoba system, after rentals paid and permanent improvements and renewals, appropriations were made in 1898, 1899, and 1900 for the construction of the Cascade Tunnel $1,950,000. F. C. 67, 799; 69, 962; 71, 659.

The Cascade Tunnel, two and one half miles in length, completed in 1900, valued by Mr. Hogeland at $2,693,535 (Portland Exhibits, p. 1445), was paid for from earnings.

An issue of $9,000,000 stock at par value was made in 1900. Annual Report, 1900, F. C. 71, 654. Market 175; value at market price $15,750,000, an extra 17½ per cent on $90,000,000 stock outstanding. There was also then provided to be issued to employes, through a trustee, $1,000,000 stock at par.

In 1901 $25,000,000 new stock, one share for every four then out, was issued. Stockholders paid $80 a share for it. The equity of each shareholder in $5,000,000 expended on improvements out of earnings was capitalized in this issue. F. C. 72, 580.

An extra dividend of 5 per cent on the par value of stock out. Market value, 203. Value of issue on basis of market, $50,750,000.

Relative to the above credit on stock issue the following official circular issued: —

"Since your company took possession of the railways and properties of the St. Paul and Manitoba Co. under the lease of February 1, 1890, it has advanced out of its revenues, for permanent additions to the same, more than $5,000,000 that has never been replaced to it. Under the provisions of that lease, framed to cover such cases, the S. P., M. & M. Ry. Co., for the purpose of acquiring the title to such additions to the extent of $5,000,000, agrees to issue its bonds to that amount. The money so advanced belonged to its stockholders and might have been paid to them in the form of dividends upon their holdings of stock but for its use in making the advances mentioned. The bonds to be issued in repayment of such advances also in equity belong to this company's stockholders. Your Board of Directors is of the opinion, however, that the interests of the stockholders

will best be subserved by this company's acquisition of said bonds for a treasury asset and their retention in the company's ownership. It has therefore been decided to acquire from the stockholders their equities in said bonds by crediting upon the subscription price of the new stock the sum of $20 per share." F. C. 72, 580.

In the annual report of 1902 appears the following admission: —

"As shown, there was applied out of the net revenue $2,000,000 to the fund for permanent improvements and renewals and there was charged against that fund $1,820,225, the cost of improvements (other than those charged to operation) made during the year to property leased from the St. Paul, M. & M. Ry. Co." F. C. 75, 914.

The annual report of the year 1904 contains the following:—

"No additional permanent capital has been obtained by this company since the issuance of $25,000,000 of capital stock in February, 1901. The amount that had been paid out by this company to June 30, 1904, on account of the purchase of securities to acquire which the said stock was issued, or advanced in anticipation of the issuance of these securities, amounted to $25,745,053 or $745,053 in excess of the proceeds of that issue. In addition to that amount the company had advanced at the same date for the construction of additional mileage, $4,501,202. There has been paid out during the three years from July 1, 1901, for additional equipment for the Northern Railway $8,241,431. There has been expended on capital account by proprietary companies $10,012,207, making the total amount paid out in three years of $48,499,894, or $23,499,894 in excess of the proceeds from the last stock issue. In addition to that amount the company has expended during the three years in additions and improvements to the property leased from the Manitoba Ry. Co., $5,114,130, out of appropriations aggregating $7,000,000 made from its revenue account." F. C. 79, 1958.

In 1905 the Great Northern Railway Company issued to its stockholders $25,000,000, increasing the stock thereby to $150,000,000. Annual Report, 1906, 5. This issue of stock was at par, and the market value of the stock, exclusive of rights, was 264. It therefore amounted to a "benefit conferred" on the stockholders, above the amount they contributed in cash of $41,000,000.

In the annual report for 1906:—

"Following the plan of previous years only such amounts as represented cost of actual additions to and improvements of the property have been charged to additions and improvements, and the entire amount charged to that account during the year on lines leased from the Manitoba Company, or $2,786,291, has been transferred to the fund for permanent improvements and renewals, so that the Great Northern Railway Company is not carrying on its books as an asset the cost of any additions to or improvements on the lines leased from the Manitoba Company. All replacements, renewals, etc., have been charged to operating expenses. The amount included in maintenance of road and structure this year for extraordinary expenditures is $2,583,054." Annual Report, 1906, 20.

These extraordinary expenditures are additions to the capital account and properly belong in the surplus.

From its income account in 1906 the company was able to appropriate $5,130,910 to "Fund for Permanent Improvements and Renewals," and "Fund for Replacement of Equipment," in addition to $10,196,087 for "Maintenance of Road and Structures," and "Maintenance of Equipment." Annual Report, 1906, 27.

The profit and loss account of the Great Northern Railway Company has yielded some noticeable results. For instance, in the annual report of 1896: —

"Interest on bonds of D. W. &. P. Railway Company prior to July 1, 1894, paid by advances made by the Great

Northern Co. in anticipation of future repayment, now charged off, $405,625." F. C. 63, 506.

In annual report of 1898, charged off Seattle & Montana system paid for from income, $6,998,619. F. C. 67, 796.

In a circular of President Hill of the Great Northern, May 25, 1898, is the following: —

"The Seattle & Montana Railroad Company owns either directly or through ownership of the entire capital stock of the local companies a continuous completed line of railway extending from Seattle northward. . . . The Seattle & Montana has no funded debt. To aid in constructing and acquiring the railways and other properties mentioned, the Great Northern Company has made advances running through a series of years and amounting on March 1, 1898, with interest, to about $11,300,000. The money forming these advances would otherwise have been subject to distribution in the form of dividends among Great Northern stockholders. In consideration of the release of this indebtedness resulting from these advances the owners of the capital stock of the Seattle & Montana have, under agreement with the Great Northern Company, transferred the whole amount of capital stock, namely, $12,500,000, in trust for the equal and ratable benefit of all the stockholders of this company." F. C. 66, 1044.

In his annual report of 1898 President Hill says: —

"As explained in the circular to shareholders, May 25, 1898, this company has from time to time advanced to the Seattle & Montana Railroad Company, to assist in the construction and acquisition of the property owned by that company, sums which with interest amounted on March 1, 1898, to $11,286,489. Of this amount the interest $4,287,869, while charged to the Seattle & Montana Railroad Company, had not been included in the Great Northern Railway Company's income account. In consideration of the issuance of the entire capital stock of the Seattle & Montana Railroad Company pro rata to the shareholders of the Great Northern

Railway Company the entire account has been written off, the balance of $6,998,619 being charged to profit and loss." F. C. 67, 796.

No bonds were issued by this Seattle & Montana Railroad Company; no capital was paid in; every dollar of the cost was taken from the earnings of the Great Northern system, *supra*. Not a dollar of capital was then put into the road as capital.

In the annual report of the Great Northern of 1902 appears this:

"Instead of purchasing the capital stock ($5,000,000) of the Seattle & Northern Company as originally intended, it was decided to buy the physical property of that company and the same was purchased as of February 1, 1902, by the Seattle & Montana Railroad Company for $1,500,000 in cash. To enable the Seattle & Montana Company to make this purchase, action was taken by stockholders to increase its capital stock from $12,500,000 to $14,000,000, the additional $1,500,000 of stock being bought by the Great Northern Railway Company." F. C. 75, 914.

Therefore the only capital stock contributed in money to any part of this Seattle & Montana system was $1,500,000, represented in the purchase of the physical property of the Seattle & Northern road. What became of the $5,000,000 of capital stock of the Seattle & Northern road when the "ownership of the physical property" passed to the Seattle & Montana Railroad Company for $1,500,000 the Great Northern balance sheet of 1906 does not show.

The above is an admission of one method of acquiring the proprietary stocks.

In the balance sheet of the Great Northern Railway Company of 1906, p. 33, among the items included in the "cost of properties controlled by the Great Northern Railway Company through ownership of the entire share capital" appears: —

Seattle & Montana Railroad, railway and equipment $20,258,455

No bonds are shown. The $1,500,000 issued in 1901 to buy the physical property of the Seattle and Northern is the only cash-paid share capital in the entire Seattle & Montana system, June 30, 1906. The rest is income of the Great Northern Railway system.

Capital paid in	$1,500,000
Cash capital per mile	$6,905
Surplus earnings capitalized per mile	$86,300
Mileage of system	217.25 miles
Capital paid in	7.4 per cent
Earnings capitalized	92.6 per cent

In annual report of 1900, charged off to profit and loss on account of securities transferred to the Lake Superior Company, Ltd., paid for from earnings, $1,851,364. F. C. 71, 659.

The imperfect history of the last item as contained in the annual reports of President Hill follows: —

"This company has from time to time become interested in properties of companies not strictly a part of the railway system, but of direct or indirect benefit to it, such as coal mines, iron mines, elevators, docks at Buffalo, N. Y., etc. It is considered that these properties can be handled to better advantage by a separate company. To this end the Lake Superior Co., Ltd. has been organized and there has been transferred to it during the year all the Great Northern's interest in the Great Northern Express Co., the Great Northern Elevator Co., Sand Coulee Coal Co. and other outside companies. The income from these properties or securities, unless reinvested, will belong to the Great Northern's shareholders. The title to these securities, etc., having by this transfer passed from the Great Northern Ry. Co. to the Lake Superior Co., trustee, the sum of $1,851,364 has been charged against profit and loss on account of part of their

cost. This will also explain why the earnings, expenditures, etc., of the Great Northern Express Co. and Sand Coulee Coal Co. have not this year been included in the revenue table as in former years." F. C. 71, 655.

Certificates of each stockholder's equitable interest in the properties thus charged off to profit and loss, having no par value, "ore certificates," represented vast holdings in the Mesabi Ore Range in Minnesota. These lands were paid for with public money, taken, through the profit and loss account, out of income and given as a gratuity, share for share, to the stockholders of the Great Northern Railway Company. Official Circular, November 22, 1906, F. C. 83, 1290.

The "ore certificates" have no par value, but were marketed at 90 when issued. F. C. 83, 1261.

The immediate "benefit conferred" on stockholders in the issue of 1,500,000 shares of ore certificates on present market value aggregated $135,000,000.

The ultimate market value has been estimated at $300 per share, or $405,000,000.

President Hill says "experts have figured the ore body 400,000,000 to 600,000,000 tons, but it would not be surprising if operations should uncover 1,000,000,000 tons." F. C. 83, 969.

The contract with the United States Steel Corporation is $1.65 per ton for the ore delivered at upper lake docks, 750,000 tons minimum taking in first year. Then an annual increase by 750,000 tons and an increase in price of 3.4 cents per ton until the output has reached 8,250,000 tons and then on that basis. It is a perpetual lease until the ore is exhausted. Judge GARY for United States Steel Corporation, F. C. 83, 822.

An output of 600,000,000 tons will yield the certificate holders $1,186,400,000. President Hill would not be surprised if the operations uncovered 1,000,000,000 tons. The

price is for ore delivered at upper lake docks. The output above my computation on 600,000,000 tons to the point of Mr. Hill's maximum will pay the cost of transportation and interest charges and leave the above profit.

This ore property was paid for with excess earnings of the Great Northern Railway Company, and presented to stockholders.

Then in 1906, also, came the last issue to date of undervalued shares, an issue of $60,000,000 of stock, F. C. 83, 1469, worth in the market, above the ore certificates, $240 per share, an undervaluation of $84,000,000.

A list of these undervaluations, from the reorganization of the St. Paul, Minneapolis & Manitoba system, in 1879, whose shareholders, and those holding under them, are the shareholders of the Great Northern Railway Company of the present date (July 1, 1907); and a table in which is shown the dividends and interest on undervalued bonds follows: —

UNDERVALUED STOCK AND BONDS ISSUED TO THE ST. PAUL, MINNEAPOLIS & MANITOBA AND GREAT NORTHERN RAILWAY COMPANIES' STOCKHOLDERS, 1879 TO 1906, INCLUSIVE.

	Consideration to corporation in cash	"Benefit conferred" on stockholders
St. Paul, Minneapolis & Manitoba.		
1879 Original issue St. Paul, Minneapolis & Manitoba stock, water		$15,000,000
1882 Stock at par, market value 140	$5,000,000	2,000,000
1883 Bonds 6 per cent at 10, par 100	1,000,000	9,000,000
1888 Bonds 5 per cent, at 75, par 100	6,000,000	2,000 000
Great Northern.		
1890 Stock at 50, market value 71	10,000,000	4,200,000
1892 Bonds at 72½, par 100	10,875,000	4,125,000
1893 Stock at 100, market 140	5,000,000	2,000,000
1898 Stock at 60, market 180	15,000,000	30,000,000
1898 Stock in exchange St. Paul, Minneapolis & Manitoba, market 192		28,000,000
1899 Stock at 100, market 190	15,000,000	13,500,000
1899 Stock at 100, market 175	9,000,000	6,750,000
1901 Stock at 80, market 203	20,000,000	30,750,000
1905 Stock at 100, market 264, exclusive of rights	25,000,000	41,000,000
1906 Stock at 100, market (exclusive of ore certificates), 240	60,000,000	84,000,000
1906 Ore certificates at 90		135,000,000
Corporation received on these issues	$181,875,000	
Immediate "benefits conferred" on stockholders, in addition to dividends		$407,325,000

RETURNS TO STOCKHOLDERS OF GREAT NORTHERN RAILWAY, 1890–1906:

	Amount of stock out	Dividends on stock	Int. on undervalued bonds	"Benefits conferred"	Total returns	Per cent
1890	$20,000,000	$200,000	$540,000	$4,200,000	$4,940,000	24.70
1891	20,000,000	450,000	540,000		990,000	4.95
1892	20,000,000	1,000,000	540,000	4,125,000	5,665,000	28.32
1893	20,000,000	1,000,000	540,000	2,000,000	3,540,000	17.70
1894	25,000,000	1,187,500	540,000		1,727,500	6.90
1895	25,000,000	1,250,000	540,000		1,790,000	7.16
1896	25,000,000	1,250,000	540,000		1,790,000	7.16
1897	25,000,000	1,250,000	540,000		1,790,000	7.16
1898	25,000,000	1,500,000	540,000	58,000,000	60,040,000	240.14
1899	90,000,000	3,851,033	540,000	20,250,000	24,641,033	27.37
1900	99,000,000	6,408,777	540,000		6,948,777	7.02
1901	99,000,000	6,897,369	540,000	30,750,000	38,187,369	39.58
1902	125,000,000	8,225,920	540,000		8,765,920	7.01
1903	125,000,000	8,673,973	540,000		9,213,973	7.37
1904	125,000,000	8,683,925	540,000		9,223,925	7.37
1905	125,000,000	8,693,860	540,000	41,000,000	50,233,860	40.18
1906	150,000,000	9,148,520	540,000	219,000,000	228,688,520	162.46
		$69,670,879	$9,180,000	$379,325,000	$458,175,879	
"Benefit conferred" on Great Northern stockholders as stockholders of St. Paul, Minneapolis & Manitoba Railway and those holding under them, *supra*				28,000,000	28,000,000	
				$407,325,000	$486,175,879	

ADMITTED SURPLUS GREAT NORTHERN RAILWAY COMPANY, 1890–1906, ANNUAL REPORTS

Years	Admitted surplus	Permanent improvements	Extraordinary expenditures	Total surplus
1890	$413,528			$413,528
1891	988,621	$100,000		1,088,621
1892	943,475	750,000		1,693,475
1893	1,182,330			1,182,330
1894	Deficiency [1]			Deficiency
1895	189,508			189,508
1896	1,042,547			1,042,547
1897	1,207,267			1,207,267
1898	2,071,768	2,250,000		4,321,768
1899	1,787,191	1,800,000	$833,228	4,420,419
1900	2,217,763	1,800,000	1,861,874	5,879,637
1901	1,689,064		1,236,204	2,925,268
1902	2,116,990	2,000,000	1,663,612	5,780,602
1903	4,134,635	3,000,000	1,443,169	8,577,804
1904	3,432,594	2,000,000	1,410,097	6,842,691
1905	5,137,376	3,000,000	2,040,645	10,178,021
1906	5,184,569	5,130,910	2,583,054	12,898,533
	$33,739,233	$21,830,910	$13,071,883	$68,642,026
[1] Deficiency 1894				104,153

Total Grand Northern surplus put into the property 1890–1906	$68,537,873
St. Paul, Minneapolis & Manitoba surplus put into proprietary companies, *supra*, 1879–1890 .	9,279,707
	$77,817,580

Income absorbed in one way and another into the system.

This footing of capitalized surplus is only that which has been admitted.

The figures are certainly much less than the true surplus. The above figures are merely the specific admissions made in the president's annual returns. There is circumstantial

evidence to show that there is a much larger sum in the true surplus. On an estimate $100,000,000 of surplus has been capitalized in the property, and in the properties and securities of proprietary companies.

Take, for instance, the year 1901.

The gross earnings were practically the same as in the preceding year. There was a falling off in some departments and increases to offset these losses in earnings in others, Annual Report, 1901, F. C. 73, — yet the surplus admitted shows a decrease from 1900 of $2,900,000.

According to the testimony of Ex-Governor McGraw it would appear that 1901 must have been the year in which the Seattle terminal lands were purchased. Portland Evidence, 672. This decrease of $2,900,000 in admitted surplus is probably accounted for by this purchase. The terminal and double-track tunnel appear as completed among the "Additions and Improvements" accounted for in annual report of 1906. Additions and improvements are paid from moneys which might have been paid out to the stockholders in dividends, *supra*. They are charged to the capital cost of the properties leased from the Manitoba system to the amount of $11,611,716 admitted. Balance sheet 1906, *infra*, and circumstantial evidence show much not admitted.

A portion of the admitted sum is found in the following items in balance sheet of 1906: —

"Cost of additions and improvements . . .	$11,611,716
Unexpended balance fund; permanent improvements and renewals	6,888,431
Fund replacement of equipment	4,251,051
Insurance fund	441,743
Surplus of proprietary companies	9,172,470
	$32,365,411
Profit and loss	27,603,558
	$59,968,969

of earnings which has gone into the property in one form or another in these ways for its physical and financial improvement." Editorial, F. C. 83, 1069.

The above total surplus does not include the surplus earnings of certain proprietary lines put back into the property, Great Northern Report, 1906, "other companies," pp. 26, 27, or expended in the purchase of other properties and securities, *e.g.*, on June 30, 1906, the Eastern Railway of Minnesota owned the bonds and entire share capital of the Lake Superior Terminal & Transfer Company . . $15,700

The Wilmar & Sioux Falls Railway Company owned the stock of Sioux City & Western Railway Company 2,500,000

The Minneapolis Union Railway Company owned bonds of Wisconsin Central Railway Company 247,500

And the Great Northern Railway Company owned stock and bonds and properties which cost $157,100,496

From which it deducts the securities of companies, the cost of the railway, land, equipment, elevators, etc., of which is included in the cost of properties listed in balance sheet 89,204,969

67,895,527

$70,658,727

Great Northern Report, 1906, 33.

The schedule of the above referred to securities, of par value exceeding $222,947,169, owned by the Great Northern Railway Company, acquired with stock, bonds, and income, as reported to and filed with the Commission by the company follows: —

Railway stocks ...
...apolis Western Railway
... Northern Railway
... & Pacific Railway
... & Montana Railway
... Minneapolis & Manitoba Railway
... Railway of Minnesota
... Falls Railway
... Lake Railway
... & Northern Railway
... & Navigation ...
... & Navigation ...
... Company
... & ...

ıding sub-
nefits con-

, after divi-
d been paid,
capital stock
ıivalent of 16.3
stock outstand-

plus is permitted
he present relative
ne Great Northern
ın amount exceeding
pital paid in, watered
value on property ac-
iation charges.

P. Clough

1896, In re Farmers' Loan
...ific Railway Co. *et al.*
...ent of the Great Northern
... connected with the Mani-
...acity. He was, and is, Mr.
...tial legal adviser.
...r. Grover testimony was given

...ugh's View

... Northern Railway
... have ...

Farmers Grain & Shipping Company . . .	$104,000
Spokane Falls & Northern Railway Securities .	4,381,000
Other bonds owned:	
Duluth & Superior Bridge first mortgage . .	650,000
" " " second "	289,000

"The following stocks and bonds were acquired from the St. Paul, Minneapolis & Manitoba Railway Company as subscription to this company's capital stock, same being made for the benefit of the St. Paul, Minneapolis & Manitoba Railway stockholders": —

Stocks owned:	
Minneapolis Union Railway	$500,000
Duluth, Watertown & Pacific Railway . . .	730,000
Wilmar & Sioux Falls Railway	1,500,000
Eastern Railway of Minnesota	5,000,000
Montana Central Railway	5,000,000
Northern Steamship Company	1,500,000
St. Paul Union Depot	43,750
Minneapolis Transfer Company	7,000
Lake Superior Terminal & Transportation Company	15,700
Climax Coal Company	149,000
Fort Benton Bridge Company	5,800
Bonds:	
Duluth, Watertown & Pacific Railway . . .	1,375,000
Minneapolis Transfer Railway	109,000
Town of Sandness	2,000
Town of Minnesota Falls	1,000

Report of Great Northern Railway Company to Interstate Commerce Commission, June 30, 1906, p. 27.

These securities may, in the absence of restrictive legislation, become the subject of a gratuitous stock issue in an ultimate unification of the system, thereby caring for the

increasing surplus for many years to come and adding substantially to the aggregate of "privileges" or "benefits conferred."

The admitted surplus of 1906, $12,898,533, after dividends of 7 per cent upon the capital stock had been paid, is equivalent to 9.8 per cent on the average capital stock outstanding for the fiscal year. It is the equivalent of 16.3 per cent on the $79,000,000 average capital stock outstanding for which cash has been paid in.

If the ratio of increase in admitted surplus is permitted to continue for the next fifty years, and the present relative rates are continued, there will be in the Great Northern system in 1957, capitalized earnings to an amount exceeding $2,000,000,000, and this exclusive of capital paid in, watered stock, and the legitimate increase in value on property acquired from capital paid in and depreciation charges.

Testimony of Mr. W. P. Clough

Taken at St. Paul, Minn., in July, 1896, In re Farmers' Loan and Trust Co. *v.* Northern Pacific Railway Co. *et al.*

Mr. Clough was the vice-president of the Great Northern Railway Company in 1896, and connected with the Manitoba system in an official capacity. He was, and is, Mr. Hill's chief of staff and confidential legal adviser.

On direct examination by Mr. Grover testimony was given as follows, pp. 98 and 100: —

Mr. Clough's View

"*Q.* State the earnings of the Great Northern Railway Company for the last fiscal year that you have there.

"*A.* [Referring to a paper book] I have that in the annual report, of which I will give the Commissioner a good copy. . . . This is for the fiscal year ending June 30, 1895.

"*Q.* I suppose the report for this year has not been completed.

"*A.* No, sir. This is the last year for which there is any report or for which the figures have been completed, another one will be completed probably in six weeks or such matter. [Reading] 'Earnings from freight, $10,365,031, total gross earnings $13,109,939. Operating expenses and taxes, $7,605,677. Net earnings, $5,504,262. Rentals, $5,372,590, making a surplus of $131,671 for the year.' These rentals, I will say by the way of explanation, are the fixed charges of the property. The St. Paul, Minneapolis & Manitoba Railway Company, which owns the system, has leased it to the Great Northern in consideration of a rental which will be made up of interest on its bonds and a dividend of 6 per cent per year upon its stock.

"*Q.* That is, of the Manitoba Company?

"*A.* Of the Manitoba Company only, and this is the result of the operations for the year: a surplus, above rental, of $131,671.

"*Q.* State the capitalization on which that rental is paid in the form of interest on bonds and dividends on stock.

"Mr. GRAVES. — You mean of the Manitoba Company?

"Mr. GROVER. — Yes, of the Manitoba Company.

"*A.* The bonds of the St. Paul, Minneapolis & Manitoba Company were $85,454,354; the stock was $20,000,000; total bonds and stock, $105,454,354. That covered a mileage of 3770.10 miles of main track, making the bond debt per mile of main track $22,666.34; capital stock per mile of main track, $5304.90; total stock and bonds per mile of main track, $27,971.24; interest per mile of main track, $1092.02; guaranteed dividend per mile, $318.29; total capital charges which constitute the rental per mile of main track, $1410.81.

"*Q.* State if the road during the year named was economically operated.

"*A.* Yes, sir. It was operated with very great economy.

I think that at about the lowest, if not the very lowest; I am sure the very lowest rate of any western railroad.

"*Q.* Have you knowledge from your official connection with the company and its books and accounts so that you can state whether the capitalization of $27,000 a mile represents the value of the cost of construction?

"*A.* Yes, sir. I have investigated that thoroughly. I have had occasion to, and I am satisfied that that capitalization represents more actual money put in the property than the figures. That the money cost was actually greater than the figures."

The Facts

As elsewhere submitted in this statement, *the bonds of the Manitoba system outstanding in June,* 1895, *contained* $9,000,000, *in value which the company did not receive in cash,* so that the bonds of a par value of $84,954,354 represented actual cash payments to the company of only $75,954,354. Of the $20,000,000 of stock, $15,000,000 was water issued at the promotion to the syndicate in 1879 and $5,000,000 was cash capital paid in in 1882, so that *the total amount of cash capital paid into the road to June* 30, 1895, *was only* $80,954,354 *or* $24,000,000 *less than Mr. Clough testified to.* On the basis of 3370 miles of road this was $21,473 in cash per mile of road, of which $20,153 was in bonds and $1320 in the stock.

It is also a question how much of the $8,000,000 issue of second-mortgage bonds in 1879 was money.

Revenue Account of St. Paul, Minneapolis & Manitoba Leased Lines

Year ending June 30, 1895

Gross earnings		$13,109,939
Operating expenses	$3,556,698	
Maintenance of equipment	950,937	
Maintenance of road and structures	1,909,313	
General expense	729,512	
Taxes	459,215	
		7,605,677
Net earnings		$5,504,262
From which has been paid for rentals,		
Interest on Manitoba bonds	$3,514,866	
Guaranteed stock dividends	1,200,000	
Interest on Great Northern collateral trust bonds	600,000	
Maintaining organization	6,574	
Other rentals	51,150	
		5,372,590
Surplus on St. Paul, Minneapolis & Manitoba leased lines carried to Great Northern income account		$131,671

Add to this, however, interest at 6 per cent upon $9,000,000 in bonds, for which the company did not receive cash, $540,000; rental at 6 per cent upon $15,000,000 of stock, for which the company did not receive any money, $900,000. These corrections would give a surplus of the Manitoba Railway Company for the year ending June 30, 1895, $1,571,671.

For the year ending June 30, 1896

Gross earnings		$15,297,452
Operating expenses		8,427,033
Net earnings		$6,870,419
Rentals, interest on bonds	$3,486,834	
Dividend on stock	1,200,000	
Interest on Great Northern collateral bonds	600,000	
Maintenance of organization	6,031	
Other rentals	90,150	
		5,383,015
Admitted surplus on Manitoba stock for the year ending June 30, 1896		$1,487,403

Equivalent to 7 per cent on $20,000,000 capital stock.

To this add, as above, 6 per cent upon $9,000,000 of fictitious value in bonds, $540,000; dividend paid upon $15,000,000 watered stock, $900,000, — total surplus, $2,927,403.

On cross-examination by Mr. Graves: —

"*Q.* Well, are you in doubt as to whether you make money on that basis or not?

"*A.* No, we were not making too much.

"*Q.* Well, you have no doubt but what you are making a good thing out of it, have you?

"*A.* We are not making a bit more than we have to get out of the business.

"*Q.* In other words, then, you have to have so much money?

"*A.* We have to have so much money, yes, sir, and we have to get it from our patrons; there is nobody that gives it to us.

"*Q.* And therefore you go for the people that you think have got in in a place where they can't help themselves?

"*A.* We try to arrange all of our rates as far as possible so that the business will move," p. 131.

Mr. Clough, in his testimony, gives the standard of profit for which Mr. Hill thought it worth while to do business; "We are not making a bit more than we have to get out of the business. We have to have so much money and we have to get it from our patrons."

Because in a short time, as soon as they could, — in two years' time, as it proved, — they were going to make the exchange of St. Paul, Minneapolis & Manitoba stock for Great Northern; and Great Northern stock must be made profitable and attractive. The rates were allowed to remain, the syndicate got the money it had to have, from patrons, the exchange in stock was made October, 1898, and immediately the stock went on a 7 per cent basis. The dividend increased from $1,500,000 in the year of June 30, 1898, to $3,851,033 in 1899, and $6,408,777 in 1900, an increase in dividend distribution including the former Manitoba rental of 237 per cent in two years.

And yet the time at which Mr. Clough's testimony was taken marked the close of the only lean period that the Great Northern Company has known. The railways had not recovered fully from the effects of the panic of 1893–94, which caused suspensions or reductions in dividends, and drove so many railroads into bankruptcy.

Balance Sheet, June 30, 1906

Being a consolidation of the balance sheets of that date of the St. Paul, Minneapolis & Manitoba, Great Northern, Eastern of Minnesota, Montana Central, Wilmar & Sioux Falls, Duluth, Watertown & Pacific, Seattle & Montana, Park Rapids & Leech Lake, Minneapolis Union, Minnesota Western, Dakota & Great Northern, Montana & Great Northern and Duluth Terminal Railway companies.

Assets

Railway Property.

Cost of railway, equipment, and lands owned by the Manitoba Railway Company		$129,370,062
Cost of additions and improvements made by Great Northern Railway Company to property leased from the St. Paul, Minneapolis & Manitoba Railway Company and paid for from fund for permanent improvements and renewals		11,611,716
Total cost of property leased from St. Paul, Minneapolis & Manitoba Railway Company .		$140,981,778
Cost of the following properties controlled by the Great Northern Railway Company through ownership of their entire share capital:		
Eastern Railway of Minnesota, railway, equipment, elevators, etc.	$29,596,899	
Montana Central Ry., railway and equipment	15,648,887	
Wilmar and Sioux Falls Ry., railway, equipment, and real estate	9,399,915	
Duluth, Watertown & Pacific Ry., railway	2,275,124	
Seattle & Montana R. R., railway and equipment	20,258,454	
Park Rapids & Leech Lake, railway and equipment	1,023,471	
Minnesota Union Railway, Union Depot, railway, etc.	3,166,645	
Minnesota Western Ry., railway and equipment	752,167	
Dakota & Great Northern Ry., railway	3,651,697	

Montana & Great Northern Ry., railway	3,178,568	
Cost of Duluth terminal, the bonds and entire capital stock of which are owned by Eastern Railway of Minnesota	396,541	
(Exclusive of $6,910,000 St. Paul, Minneapolis & Manitoba improvement bonds not shown *contra*)		89,348,373
Total cost of property of Great Northern Railway line		$230,330,151

Other Properties, Securities, and Investments.

Cost of stock in Lake Superior Terminal & Transfer Company owned by Eastern Railway of Minnesota	$15,700	
Cost of stock of Sioux City & Western Railway Company owned by Wilmar & Sioux Falls Railway Company	2,500,000	
Wisconsin Central Company's Minneapolis Terminal, bonds owned by Minneapolis Union Railway Company	247,500	
Cost of properties and securities owned by Great Northern Railway Company	157,100,496	
Total	$159,863,696	
Less par value of the following securities owned by Great Northern Railway Company and not shown *contra* :		
Entire capital stock of		

Eastern Railway of Minnesota .	$16,000,000	
Montana Central Railway . .	5,000,000	
Wilmar & Sioux Falls Railway .	7,000,000	
Duluth, Watertown & Pacific Railway	730,000	
Seattle & Montana	14,000,000	
Park Rapids & Leech Lake Railway	500,000	
Minneapolis Union Railway . .	500,000	
Minnesota Western Railway .	250,000	
Dakota & Great Northern Railway	2,000,000	
Montana & Great Northern Railway	7,000,000	
Entire issue bonds of Duluth, Watertown & Pacific Railway	1,375,000	
Park Rapids & Leech Lake Railway	500,000	
Total	$54,855,000	
196,530 shares stock St. Paul, Minneapolis & Manitoba . .	19,653,000	
£2,000,000 St. Paul, Minneapolis & Manitoba Pacific Extension bonds	9,696,969	
St. Paul, Minneapolis & Manitoba improvement bonds . .	5,000,000	
	$89,204,969	
Cost of properties, securities, and investments after deducting par value of stocks and bonds not shown *contra*		$70,658,727
Share of Chicago, Burlington & Quincy securities		109,113,909
Total capital assets		$410,102,788

Current Assets

Cash land department St. Paul, Minneapolis & Manitoba Railway		14,366
Cash	$13,683,809	
Due from agents, etc.	2,645,821	
Advanced charges	67,575	
Bills receivable	3,793,663	
Due from companies, etc.	3,075,622	
	$23,266,493	27,297,790
Material, etc., on hand	4,031,297	
		$437,414,945

Stock Liabilities

Capital stock Great Northern Railway Company, outstanding	$149,546,050
St. Paul, Minneapolis & Manitoba Railway stock outstanding	347,000
Total stock in hands of public	$149,893,050

Funded Debt in hands of Public

St. Paul, Minneapolis & Manitoba bonds:		
2d mortgage	$6,470,000	
Dakota Extension	4,939,000	
Consolidated 6 per cent	13,344,000	
Consolidated 4½ per cent	19,250,000	
Montana Extension	10,185,000	
Pacific Extension	19,393,939	
	$73,581,939	
Bonds proprietary companies	26,646,000	
		100,227,939
Chicago, Burlington & Quincy bonds, proportion		107,612,600
		$357,733,589

St. Paul, Minneapolis & Manitoba bonds redeemed through sinking funds		$11,925,400
Contingent Liabilities		
Cost of additions and improvements made by Great Northern Railway Company to property leased from St. Paul, Minneapolis & Manitoba Railway Company and paid for from fund for permanent improvements and renewals	$11,611,716	
Unexpended balance fund for permanent improvements and renewals	6,888,431	
Fund replacement of equipment .	4,251,051	
Insurance fund	441,743	
Surplus funds of proprietary companies deposited with Great Northern Railway Company .	9,172,469	
		32,365,411
Current and Deferred Liabilities		
Sinking fund and land department .	$14,366	
Vouchers, pay rolls, dividends, etc.	6,690,100	
Taxes, interest, and rentals accrued	1,082,519	
		7,786,985
Profit and Loss		
St. Paul, Minneapolis & Manitoba Railway Company	$2,032,104	
Great Northern Railway company .	25,571,453	
		27,603,558
		$437,414,945

Annual Report, 1906, 32, 33.

An analysis of the balance sheet of 1906 is here given:

Cash capital invested:		
Capital stock outstanding		$149,893,050
Earnings and water in stock, *infra*		45,000,000
Cash in stock, Great Northern Railway Company		$104,893,050
Bonds outstanding, Great Northern and proprietary companies	$100,227,939	
Water in bonds, *infra*	9,000,000	
Cash in bonds held by public		91,227,939
		$196,120,989
Cash from sales of lands granted by state		11,925,400
Cash premium on bonds redeemed from sinking fund		1,143,487
		$209,189,876

Cash earnings converted into capital:		
Additions from earnings to St. Paul, Minneapolis & Manitoba Railway since 1890	$11,611,716	
Unexpended fund for permanent improvements	6,888,431	
Fund for replacement of equipment	4,251,051	
Insurance fund	441,743	
Profit and loss balance, St. Paul, Minneapolis & Manitoba	2,032,104	
Profit and loss balance of Great Northern Railway Company and proprietary companies	25,571,453	
Surplus funds of proprietary companies deposited with Great Northern Company	9,172,469	
	$59,968,969	

Premium on bonds from sinking fund, as above	1,143,487	
Total earnings in balance sheet .	$58,825,481	
Not all the permanent additions appear on the balance sheet.		
Earnings in stock:		
First issue Great Northern stock 1890	10,000,000	
		$68,825,481
Water in stock:		
First issue by St. Paul, Minneapolis & Manitoba, 1879 (bought with fourth stock issue of Great Northern in 1898)	$15,000,000	
Third issue by Great Northern, 1898 (Seattle & Montana) . .	10,000,000	
Fourth issue, 1898 (premium on St. Paul, Minneapolis & Manitoba stock)	5,000,000	
Eighth issue, 1901 (additions to St. Paul, Minneapolis & Manitoba paid for with improvement bonds)	5,000,000	
Total water in stock	$35,000,000	
Bonds:		
$10,000,000 consolidated mortgage bonds (issued at 10) in 1883 . .	9,000,000	
Total water in capital		$44,000,000
(Exclusive of second mortgage bonds, $8,000,000)		

Total Great Northern capital in balance sheet .	$322,015,357
Current and deferred liabilities	7,786,986
Chicago, Burlington & Quincy bonds . . .	107,612,600
Total of 1906 balance sheet	$437,414,945

The property thus acquired is as follows: —

Cost of railway, equipment, and lands of St. Paul, Minneapolis & Manitoba Railway, including cost of additions and improvements	$140,981,778
Cost of properties controlled by Great Northern through ownership of entire share capital	89,348,373
Cost of other properties, securities, and investments less par value of stocks and bonds of above companies	70,658,727
Bills receivable	3,793,663
Due from other companies, etc.	5,789,019
Material and fuel on hand	4,031,297
Cash on hand	13,698,175
Cost of securities Chicago, Burlington & Quincy	109,113,909
	$437,414,945

The earnings represented herein may be traced to revenue and income account, *supra*.

Capital invested in Great Northern system, exclusive of Chicago, Burlington & Quincy stock	$209,189,876	— 64.9 per cent
Earnings converted	68,825,482	— 21.4 per cent
Water in capital	44,000,000	— 13.7 per cent
Mileage, June 30, 1906		6,635.34 miles
Invested capital		$31,526 per mile
Capital, including converted earnings		$41,899 per mile

Right of way obtained by grant from the state of Minnesota, also under Act of Congress, 1875, *supra*, based on Mr. Hayden's testimony.

Portland Exhibit, 1478.

Minnesota, 139.88 miles, $279 per acre	$1,023,930
Minnesota, 62.95 miles, $279 per acre	460,629
North Dakota, 316.57 miles, $301 per acre	2,431,177

South Dakota, 17.55 miles, $355 per acre . .	163,300
Montana, 524.40 miles, $111 per acre . . .	1,527,360
Idaho, 27.41 miles, $250 per acre	176,750
Washington, 78 miles, $209 per acre	426,623
	$6,209,769

In 1896 this syndicate, represented by Mr. Hill and Lord Mount Stephen, purchased a third interest in the stock and with it control of the Northern Pacific Railway, 258,341 shares in issues of 800,000 shares. The price paid was $16 per share, paying $4,133,456 for a present 7 per cent stock, par $25,834,100, and of greater market value at the present day. Mr. Adams' first brief, 71. This purchase stands as a part of the profits of this syndicate. The importance of this purchase lies in the fact that it gave this syndicate control of $200,000,000 of railroad property in the Northern Pacific system and enabled the syndicate to control rates.

TWENTY-SEVEN YEARS OF SYNDICATE ADMINISTRATION.
1879–1906

The Fruits:

Unsold granted land 182,000 acres	not valued
The Great Northern Railway system as valued by the syndicate, Portland Exhibits, 1474 .	$414,779,917
Cost of stocks and bonds owned less par value of those whose property value is represented in cost of Great Northern property, 1906 Report, 33	70,658,727
Half interest in Chicago, Burlington & Quincy securities	109,113,909
Increase in value C., B. & Q.	not valued
One-third interest in Northern Pacific . . .	66,000,000
Ore property above transportation . . .	1,186,400,000
Portland, Spokane and Seattle Railway . .	not valued
	$1,846,952,553

The cost:		
First investment in 1879 (returned in full from sale of lands granted by the state), with which the syndicate secured its holdings .		$6,780,000
Capital since invested by syndicate and public:		
In stock	$104,893,050	
In bonds	91,227,939	
		196,120,989
Lands sold beyond the redemption of above bonds		6,288,887
Total investment in Great Northern properties		$209,189,876
Invested in 1896 for control of Northern Pacific		4,133,456
Chicago, Burlington & Quincy bonds, half interest		107,612,600
		$320,935,932
Profits of 27 years		$1,526,016,621

The Great Northern system of railways is well managed. It has been economically managed. No money has been wasted in operating expenses, none in salaries, none in interest on securities offered to the public.

For 6450 days' work in 1906 the Great Northern Railway Company paid its general officers $144,000, an average of $22 per day; much less than other large railway systems. The chief, Mr. Hill, receives no salary.

The interest paid on bonds is conservative, varying from 4 to 6 per cent.

Conclusions

Mr. Hill has paid out in dividends $69,000,000 (page 111). His surplus earnings amounted to another $69,000,000 (page 112).

He pays in dividends 7 per cent.

He might have paid on all stock (cash, earnings and water) twice as much (page 112).

When Mr. Hill borrows from the public he pays 5 per cent interest. An. Rep. 1906, 32.

When Mr. Hill borrows from his syndicate he pays 60 per cent; he pays $600,000 of interest annually on $1,000,000 borrowed through an issue of $10,000,000 of 6 per cent bonds at 10 cents on the dollar (pages 81 and 82.)

When Mr. Hill borrows from the public he pays this:

1 or 5%

When he borrows from the syndicate he pays this:

1 2 3 4 5 6 7 8 9 10 11 12 or 60%

The cash invested in capital stock, June 30, 1906, amounted to $104,893,050 (page 128); the dividend of 1906 amounted to $9,148,520 (page 111). The dividend rate on the cash invested was 8.7 per cent.

These are the syndicate's pocket money. The real return to the syndicate is this: —

Mr. Hill acquired with money taken from earnings of the railways the Mesabi ore properties (page 107); the beneficial interest thereon he has distributed among the shareholders of the Great Northern Railway Co., share for share. The immediate market value of these ore certificates at the date of issue at 90 was $135,000,000 (page 109). In other words Mr. Hill has already returned to the shareholders, exclusive of dividends and on this one transaction, every dollar of capital stock they have ever paid in with $30,000,000 more, exclusive of dividends and other "benefits."

He holds to-day, in the Great Northern system, property which, exclusive of the stocks, bonds and other securities owned, he values at $414,779,917 (page 131). Against this and the only capital lien that can be shown contra are bonds on which the public has loaned $91,227,939 (page 128), a

clear surplus in the Great Northern property alone of $323,-551,978.

All this is exclusive of stocks and bonds of the par value of $222,947,169 (page 115) which list although given as filed with the Commission does not include all the securities so owned. (See 1906 Annual Report to Stockholders, 28, 29, as to income on Nelson & Ft. Sheppard, Columbia & Red Mountain and Red Mountain Ry. Co., "interest on bonds owned $108,060" which represents at 5 per cent interest the sum of $2,161,200 of securities owned and not included in the list given the Commission.) The securities listed do not include other properties, coal mines, elevators, etc., owned by the Great Northern Ry. Co. or held in trust for the shareholders thereof, June 30, 1906. Included in such properties are the Sand Coulee Coal Co., the Great Northern Express Co., etc. (page 107), the legal title to which is elsewhere than in the Great Northern Ry. Co., and which are not included in the reports of operation for 1906, but the value of which doubtless exceeds $200,000,000. The equitable title to all this property "not strictly a part of the railway system, but of direct or indirect benefit to it," is in the shareholders of the Great Northern Ry. Co. It was paid for with the assets of the Great Northern System (page 107).

The lease to the United States Steel Corporation under which the lessee is to take a minimum of 750,000 tons of ore, increasing 750,000 tons annually to a stated point and then on until the ore is exhausted (page 108), is an attempt to control the output and price of steel, a conspiracy to monopolize the steel market. Here the monopolies, the Great Northern Ry. Co. and the U. S. Steel Corporation, converge, the lease being perpetual and the Great Northern Railway Co. having the transportation of the ore taken thereunder to the exclusion of all competition, in defiance of the Act of 1890, the act for the regulation of monopolies and of restraints of trade. The shareholders of the Great Northern

Co. HAVE not only received back their entire contribution to the stock in full and 30,000,000 dollars more, exclusive of dividends, but they WILL receive the great benefit arising from an exclusive contract for hauling this vast body of 1,000,000,000 tons of ore (page 108).

Mr. Hill has to this point, 1906, succeeded not only in returning to the shareholders $69,000,000 in dividends; in paying $9,000,000 to the syndicate in 60 per cent interest on $10,000,000 of gilt-edge 6 per cent bonds issued at ten cents on the dollar (page 81); returning to them every dollar of share capital they have ever paid in and $30,000,000 more through the distribution of ore certificates, but every five years on an average he has doubled the value of the property and in addition laid aside for future digestion a handsome nest egg in the form of securities and properties, worth apparently as much as the railway system itself.

Mr. Hill agreed in 1883 to so adjust differences with his competitors as to prevent disastrous competition (page 82), and he has lived up to his agreement.

He has not only done as he agreed but in the doing he has pulled his weakest competitor up to the 10 per cent dividend level. In the process Mr. Hill has accumulated more than $1,800,000,000 in railway properties, mines, and securities (page 131).

He appears now for the first time to be getting his administrative machinery into effective working condition.

FREDERICK O. DOWNES.

No man can lay the last balance sheets contained in the foregoing analysis beside the first, and then examine the causes which have produced this progressive increment of capital, without perceiving that the issue of the monopolistic administration of our railways does, veritably, touch the national sovereignty.

And here I wish to pause a moment to recall precisely what sovereignty means. Sovereignty signifies not only that the sovereign actually possesses the whole common property of the community he governs, but that, through taxation and eminent domain, he has the potential possession of the entire property of each individual among his subjects. That consolidated capital, if permitted to use sovereign powers in aid of monopolistic administrative methods, will attain to this supremacy within a relatively short period, is a problem which, in its economic aspect, may be demonstrated mathematically.

Given the factors as they are given in Mr. Hill's reports, and in other official documents, and assuming that the rate of progression in the future shall only be that which has obtained in the past, instead of undergoing steady acceleration, and it is easy to calculate the somewhat brief period which must intervene before all the railways of the Union shall pass under the irresponsible control of a narrowing body of capitalists.

Also the position which those capitalists must hold, if order is to be kept, may be defined with some precision. To succeed they must first destroy the public trust, since the monopolistic system is based upon discrimination according to powers of resistance, and the trust is based upon the

theory of equality before the law. But discrimination by the sovereign among subjects, according to strength, ends logically in slavery, for slavery is only the confiscation of the bodies of the weak to the private use of the strong, after their property has first been seized. Admitting that monopolists would find it neither desirable nor profitable to push discrimination and confiscation to slavery, yet they would have to push their system far enough to discriminate at will, in order that they might be free to find the maximum function of their two variables, the variable of price and the variable of sales, in relation to human movement.

To annihilate the trust would place at their disposal, as arbitrary sovereigns, the whole property of the community, for the power to tax, as Chief Justice MARSHALL explained long ago, is the power to destroy, while the impost on movement is the most searching, as the monopolistic price is the most discriminating, of taxes.

All these conclusions are the logical deductions from Mr. Hill's own statements, or the statements of counsel on his behalf, in this cause. He has asserted his lawful right to impose the monopolistic price upon those who use his highways, and to appropriate to his own use, free from all accountability, the whole surplus proceeds of this tax.

In order to attain to and hold this supremacy the body of monopolists who control movement must dispose of ample physical force, for, since human society first cohered, men have never willingly consented to being deprived of their property at the arbitrary will of another, or for his private use. If they have submitted to such usage they have only submitted through necessity. Therefore, when the monopolistic methods of administration have yielded their ultimate effects, the machinery of government which we know, such as president and congress, governors, legislatures, and courts, will have become a formal instrument serving as a mask to protect a sovereign oligarchy, whose authority must rest

upon coercion and not upon consent. So far as history serves to guide us, but one method has been devised through which the working of natural selection, which provides for the ascendancy of the strongest and the slavery of the weakest, can be regulated. That method is the institution of a public trust similar to Magna Charta. The substance of such a trust is that all men shall stand equal before the law of their country, or, in words of Locke, that there shall be "one rule for the rich and the poor, for the favorite at court and the countryman at plough."

This is the trust which the city of Spokane now prays your Honors to enforce against these defendants, standing as you do, the representative of the guardian of the whole American people.

I apprehend that the legal principles upon which this trust should be enforced, if the trust is to stand, are clear beyond controversy.

The defendants themselves have proved that, by the imposition of the monopolistic price upon those who use their railways, they draw annually from the citizens of Spokane, who live under monopoly, about $1,000,000 more than they draw from the same number of persons, for the same or for cheaper service, who live where competition prevails.

This $1,000,000 of excess of taxation over their proportionate contribution to the maintenance of the highways, represents the imposition of an undue burden very considerably over $10 annually upon every man, woman, and child in Spokane. It is worth while to reflect on what this means. The whole internal revenue collected in 1906 *per capita* in the United States, plus the whole customs revenue *per capita*, came to only $6.43. The value of the total exports of the United States is but $20.40 *per capita*. The *per capita* levies by the States of ad valorem taxes averaged, for the whole United States, $9.19, as shown by the last census.

The evidence shows that this disproportionate contribution toward the highway tax is devoted either to swell directly the emolument of a government agent already more than reasonably paid, or else that it is appropriated, as the defendants maintain that it should be appropriated, to the construction and permanent improvement of public works used by the citizens of the coast equally with the citizens of Spokane.

I submit that such a use of surplus earnings is a breach of the public trust. Primarily, surplus should be used neither to improve highways, which are a common burden, nor for the emolument of trustees above their minimum compensation, but for the equalization of the incidence of the highway impost. Also I apprehend that this interpretation of the law coincides with the decisions of the Supreme Court, so far as those decisions can be urged as an approval of discriminations in the imposition of railway rates. Possibly the leading decision in the line of cases to which I allude is that of the Interstate Commerce Commission *v.* Alabama Midland Ry. Co., 168 U. S., 144; the last, in order of time, was Interstate Commerce Commission *v.* Louisville & Nashville, 190 U. S., 273.

These litigations are not, indeed, very material to the present controversy, for they did not turn upon the constitutional question of discriminating taxation. They turned upon the meaning of two words in Section 4 of the Act of 1887 Regulating Commerce. The fourth clause of that act provided for the equalization of rates between terminal and lesser distance points, when the conditions prevailing at the terminal and at the lesser distance points should be similar. The Court held that persons living under servitude to monopoly, live under conditions dissimilar to those under which persons live who may contract freely. This, though it may be a sad, is an incontrovertible fact. The Supreme Court therefore held that where such dissimilarity of con-

dition exists the statute does not apply. Further than this the Court did not go.

The principle thus laid down is foreign to the principle on which the plaintiffs rest their case. This complaint is brought under the fifteenth clause of the Act of 1887, to Regulate Commerce, as amended by Section 4 of Chapter 3591 of the Acts of 1906. This clause gives this Commission power to prescribe what shall be reasonable rates and practices for the regulation of railroads. The contention of the plaintiffs is that *prima facie* all men should receive equal service from a government agent for an equal payment, and if such equality of service is not rendered it is evidence of unreasonableness only to be overcome by proof of controlling necessity.

Such necessity might be a failure of revenue to support the highway were the rule of equality enforced.

For example, supposing it to be proved that competition at a terminal had forced rates at that terminal to a point which would deprive the agent of compensation, or even bankrupt the line, were the rates at the terminal made the standard for all less distances, it might be held to be reasonable that the greater good of the greater number demanded a sacrifice from the population under monopoly from whom alone the necessary funds could be collected. It is precisely to obviate the occurrence of such a contingency that the President has advised Congress to exempt railways from the operation of the Sherman law, in order that, by reasonable agreements to maintain rates at terminals, undue depression of prices by competition may be prevented.

In this case it is not denied that an agreement to maintain prices at terminals does, in effect, exist, Spokane Evidence, vol. I, p. 20, although such a concerted policy is probably criminal. Nevertheless, the existence of concerted action to control prices would preclude the railways from setting up the argument of the inadequacy of terminal rates

to support the corporations, even were their treasuries less plethoric than they are. In the face of the surpluses shown in the reports, such a pretension would be preposterous, nor do I understand that it is seriously made. What I apprehend to be the position assumed by the defendants is this: They maintain that it is lawful for railway companies to levy unequal imposts, upon the population subject to their monopoly, for the purpose of raising revenue for their own emolument or for the purpose of improving and constructing highways, provided that those subject to such imposts cannot prove the rates to be intrinsically unreasonable, or unreasonable in and of themselves.

Were this proposition to be established as law, I am inclined to think that the ultimate triumph of the monopolistic system of administration would be assured, for it is doubtful if any rate could ever be demonstrated to be intrinsically unreasonable, or unreasonable in and of itself. Reasonableness, indeed, necessarily implies a comparison, for nothing can be shown to be reasonable without reference to something else which is unreasonable. In fine, reasonableness is a mental conception based on an average, whereas unreasonableness is deviation from an average. Therefore probably no rate could be shown to be unreasonable in default of some external standard whereby to measure what is reasonable.

Assuming these premises to be sound, the complainants submit that one standard of reasonableness, at least, is furnished by the principles of the public trust, and by the provisions of the Constitution of the United States which are declaratory of that trust.

The Constitution has ordained that imposts and excises shall be uniform. The axiom of the trust is that men shall be equal before the law, irrespective of wealth or poverty, of weakness or of strength.

Unless these deductions can be shaken, it follows inexorably that it is both unlawful and unreasonable to raise

more money for the use of a public work from a certain class of the population, because that class is under servitude to monopoly and cannot resist, than is raised from a more fortunate class which is free, unless necessity requires the sacrifice. Far more is it unlawful and unreasonable to raise one single dollar by such taxation to increase the emoluments of government agents who already enjoy reasonable compensation.

It is as unlawful and as unreasonable to raise surplus revenue in the manner aforesaid, to be applied to the uses I have indicated, as it would be to take private property for a public work under the power of eminent domain, and refuse compensation therefor, and it would be unlawful and unreasonable for the same cause.

As the Court of Appeals of New York has explained, a tax exacts money from individuals as and for their respective shares of contribution to any public burden. Private property, taken for the public use by eminent domain, is not taken as the owner's share of contribution to a public burden, but as so much beyond his share. Therefore, the excess is made good to him. The People *v.* The Mayor of Brooklyn, 4 N. Y., 422, 423.

But, by the exaction of the monopolistic price from the citizens of Spokane for use of the highways, over ten dollars each year is taken from every inhabitant of the town above their proportionate share of contribution to the transportation impost, and this without the excuse of necessity. The same is true, in greater or less degree, of every citizen of the Northwest who lies under servitude to the railway monopoly.

As a conclusion to this chain of reasoning, the complainants pray your Honors to rule as follows: That, where the incidence of the transportation impost is unequal, for the same service, as between different communities, the standard of reasonableness for the regulation of rates shall be equality; therefore, that the first application of surplus income shall

be toward the equalization of the incidence of said impost on transportation, between such communities as stand on an inequality for like service. I urge this ruling upon your Honors with emphasis because I apprehend that here lies the line of cleavage between public-service railway administration and monopolistic railway administration.

The monopolistic system hinges upon one proposition: that it is competent for a government agent, administering highways, to discriminate between classes of citizens, in order that he may raise surplus revenue to convert into private capital, thus causing his own private property to increase in the geometrical ratio by the appropriation of money, raised by the interposition of the sovereign, to a private use.

The prize before the monopolist is so dazzling as possibly, in their view, to warrant the adoption of any expedient, however seemingly fatuous, which offers even the faintest prospect of success. That prize is no less than the possibility of absorbing the whole national wealth; and, in view of the end to be attained, even the fantastic propositions relating to valuation advanced by these defendants take a sinister import. They are an effort to fix upon this country the monopolistic price.

Turning now from the contemplation of the effects of permitting the monopolistic system of administration to spread throughout the Union, I come to the consideration of the different aspects in which the ruling for which I ask may be scrutinized, and I submit that, whether it be presented as a legal, an economic, or a political proposition, it has the solidity of an axiom.

As a proposition of law, the ruling hardly admits of criticism, for the cornerstone of constitutional government is equality in proportionate contribution to public burdens, and compensation to him from whom more is exacted for a public object than his proportionate share.

As a proposition of economics, the ruling is equally incon-

trovertible, since all economists agree that perhaps the greatest administrative achievement of modern times has been the abolition of oppressive and unequal exactions upon the highways, and the equalization of the cost of maintenance thereof. A chief part of this reform has been the suppression of hateful taxation which imposed a servitude upon the weakest portion of the population for the benefit of the favored classes, by constraining the peasantry to labor gratuitously upon the public ways.

That the ruling is sound political policy is self-evident. The worst convulsions which have rent society have been those which have been caused by the effort of the weak to free themselves from unequal exactions imposed upon them by the strong. I have already cited several famous causes which have involved this issue, such as the Ship Money and the Writs of Assistance; and in these controversies the courts have not always shone in the fairest light in the eyes of posterity. The reason has been that courts have seldom appreciated the gravity of the danger until too late.

There are few graver menaces to the public peace than discriminating taxation, because a discriminating tax creates a favored class eager to defend its privilege, whereas oppressive but equal taxation is universally resisted. This creation of a reactionary class, by means of discriminating taxation, has been a fruitful cause of revolutions and of civil wars. Discriminating taxation was the determining cause of the revolt in France in 1789, as it has been the determining cause of the anarchy in Russia.

Extortionate rates imposed equally by the railways of the Union would be corrected forthwith, since the whole population would resist them; but discriminating rates are upheld by those who gain by them, and these are usually, for the time being, the strongest. Your Honors will hardly find a more noteworthy example of this phenomenon than that of the attitude of the interveners in this litigation.

Bodies of merchants representing the cities of the Pacific coast, many times more populous, more powerful, and more opulent than Spokane, have intervened to prevent the granting of relief to Spokane, and to the whole interior of the Northwest, lest the citizens of those coast cities should thereby be made to assume their proportionate share of the public burdens, and possibly also to forego certain advantages which they reap by discrimination in their favor on the national highways.

At the first hearing at Spokane the interveners appeared and filed a petition objecting to the granting of the prayer of Spokane, because water competition existed at the coast, which justified the policy of the railways in granting lower rates to the coast than were granted to the interior where monopoly prevailed.

When Spokane freely admitted water competition, but supported its prayers for relief by such arguments as those which I now adduce, the interveners broadened their ground, and, without abandoning their claim to preference because of the natural advantages of their position, asked leave at Portland to file a supplementary petition, praying that rates from west to east, as well as rates from east to west, should be considered, because the rates from west to east were intrinsically too high, and all the rates of these railways formed an indissoluble whole, which could not be dealt with in detail. With your Honors' permission, I have a few words to say touching these two petitions, as they have a vital bearing on the complexion of this controversy. In treating them I shall take them up in the reverse order, considering the second first. I feel the more at liberty to do so as, though the second petition was very properly dismissed at Portland, its substance was pretty fully argued at Washington, and there I had no opportunity to reply.

In answer to the allegation that the rates from west to east are excessive, I have no objection to admit, on behalf

of the petitioners, that these rates are unreasonable, but I insist that, in this controversy, the mere intrinsic amount of any particular charge is relatively unimportant. The substance of the issue now presented to your Honors is the constitutional wrong of an unequal imposition of taxation, rather than a dispute as to the amount to be paid upon any specific schedule.

In their second petition the interveners sought to interpolate a new controversy, relative to rates from west to east, which is a question purely of discretion. The sum of money to be raised by taxation, otherwise equal and lawful, is a matter of policy. Inequality of taxation infringes a constitutional right. The city of Spokane would be pleased to see the cities of the coast file a bill for the amelioration of the rates from west to east, as an independent proceeding, but the city of Spokane insists that all complaints as to merely excessive charges, which bear equally on all, should be postponed to the redress of grievances which bear upon a single class. Now it is an undisputed fact that, whether or not the rates from west to east be too high, they are equal and logical rates.

I took care to establish this proposition at the hearing at Portland, and the evidence was not controverted. Mr. Woodworth testified, in answer to my questions, that they, the rates from west to east, "are clean and consistent tariffs," and "progress on the basis of distance." Portland Evidence, pp. 851, 852. The distinction between such rates and those of which Spokane complains is palpable. The rates from the coast to the east may be too high, and so work hardship, but they are an equal burden on all, and surplus collected by such an impost may be lawfully expended upon a highway, since the surplus is the product of an equal tax, and the highway is a public work.

Therefore the question of the rates from west to east is a question of policy only; the question of rates from east

to west is a question of right. Evidently the redress of a constitutional wrong should precede the redress of an undue, but equal and lawful impost.

Passing now to the interveners' first petition, I have a graver remonstrance to address to this tribunal. The interveners have seriously maintained that competition at the coast not only justifies lower rates to the coast than those given to the interior under monopoly, when it can be proved that some overruling exigency requires such a discrimination; but they have gone further, they have insisted that this advantage of position gives those enjoying that position a right to have this advantage recognized in the payments they make toward the construction and maintenance of public works.

Being struck with the attitude of the interveners at the hearing at Spokane, I took pains at Portland to ascertain the precise position of these cities from their witnesses. Accordingly, to be perfectly fair, I asked the witnesses successively, whether they would be willing to accept the principle of the Long and Short Haul, which is the principle of equality, if it were applied by the defendant roads in their own case, precisely as it is applied by the Pennsylvania and other eastern roads to the eastern seaports.

I observed a general reluctance, both on the part of witnesses and counsel, to meet this issue frankly. Sometimes they pretended that they did not understand what the principle of the Long and Short Haul was; sometimes, like their counsel Mr. Teal, who repeatedly interposed to aid his witnesses, they intimated that the adoption of the Long and Short Haul would make no difference; and sometimes they insisted that to enforce it would be impossible. Portland Evidence, p. 738. Finally, I came to a point with Mr. Mears, who represented the Portland Chamber of Commerce, and was the chief witness for the interveners. I was the better satisfied with this as Mr. Mears is a man of courage and

capacity, who is Secretary of the Transportation Committee of the Portland Chamber of Commerce, and spoke, with unhesitating authority, the views of his principals. I quote his words touching this matter:

"Mr. ADAMS. — Would you be willing to have the Long and Short Haul clause enforced in this country?

"Mr. MEARS. — Certainly not. . . . It is utterly impossible to enforce it, Mr. Adams.

"Mr. ADAMS. — I was not asking whether it was possible or impossible. The theory of the Long and Short Haul is in use on the Pennsylvania system; it is in use on every eastern system. Now would you be willing to have the eastern system introduced here?

"Mr. TEAL. — What difference would it be?

"Commissioner PROUTY. — I understood him to say he would not be.

"Mr. ADAMS. — He said he did not understand.

"Mr. MEARS. — I say now that I would not.

"Mr. ADAMS. — That is to say, you want to have a discrimination in your favor?

"Mr. MEARS. — I want to have that distinction which geographical position gives us." Portland Evidence, pp. 738, 739.

If I apprehend Mr. Teal's argument at Washington correctly, he substantially reaffirmed this position of Mr. Mears. The Pacific Ocean, Mr. Teal averred, is the only natural advantage which Providence has given Portland, and that advantage must not be abridged even if its continuance throws upon others the burden of the highway tax which Portland might otherwise be constrained to pay.

I need hardly point out that this is but a new incarnation of the spirit of the old attacks upon the trust, the old attacks of the Ship Money and the Writs of Assistance; but, however incarnated, the animus is changeless. The strong forever seek to prey upon the weak, and always strive to use

the power of the sovereign to attain their end. The justification never varies. It is that God has decreed that men shall be unequal. In this case, in order to retain an exemption from imposts, these cities form an alliance with the railways, the greatest social power in the world, to fix the monopolistic system of administration upon the United States. They decline to contemplate the fact that when the monopolistic principle is once established they too shall pass under servitude.

Among the multitude of examples which rush upon the memory to illustrate this fatal tendency, I recall one which is singularly apposite, since it is the prototype of this intervention and of the pretension of the cities of the coast. Perhaps of all the oppressive and discriminating imposts which were the characteristic of the old French monarchy, the most hateful was the corvée, which threw upon the peasantry the whole burden of the highway tax by constraining them to labor on the roads without compensation.

In August, 1761, Turgot was appointed Intendant of the Généralité of Limoges, which he found plunged in direst poverty. Contemplating the problem of alleviating the distress, Turgot concluded that he could do nothing more effective than to suppress the corvée, and substitute therefor road building by equal taxation. In a degree he succeeded. Also his administration was brilliant, — so much so that after refusing several offers of promotion, that he might complete his task, the King nominated him, in July, 1774, Minister of Marine. The following August he became Minister of Finance. In January, 1776, he presented to the King six edicts, the first of which was, perhaps, the most celebrated act of his life. It was the edict for the suppression of the corvée throughout France, and the substitution therefor of a general highway tax.

Turgot explained in this edict, in the name of the King, the economic and legal reasons which actuated him in making

this innovation; and a few sentences from this famous state paper are not without their interest here:—

"The utility of roads destined to facilitate the transport of merchandise, has been recognized in all times. Our predecessors have regarded the construction and the maintenance of roads as one of the objects most worthy of their vigilance."

After this introduction, Turgot entered into an economic discussion, too long to be extracted, but which is as sound sense now as it was then. After summing up this side of this argument, he continued: —

"These different motives suffice to make us prefer to the corvée, the gentler and the cheaper means of building roads for money payments [instead of by forced labor], but a motive more powerful and more decisive still decides us; it is the injustice inseparable from the use of corvées. . . .

"Men have been alarmed at the expense which the construction of roads by a tax in money would cause. . . .

"They have feared to impose this tax on the people always too burdened; and have preferred to demand from them gratuitous labor, . . . rather than money which they had not.

"Those who reason thus forget that the government should not demand from those who have only their hands, either the money which they have not, or the hands which are their only means of feeding themselves and their families. They forget that the corvée is itself an impost, and an impost much heavier, much more unequal, and much more crushing than that which they fear to establish." Œuvres de Turgot, Paris, 1809, vol. VIII, pp. 273, 280, 285, 287.

No sooner was this edict promulgated than every selfish interest in France awoke. To become binding, the edict had to be registered by the Parliament of Paris, the highest court of the kingdom. The jurists of Parliament first prepared a remonstrance, and then, having chosen a deputation from their body to represent them, sent the deputation,

charged with the remonstrance, to meet the King at Versailles. Bearing in mind that the edict was intended to relieve the most oppressed part of the population from the most discriminating and noxious tax of Europe, the whole remonstrance is illuminating. I quote a single paragraph to show how the French bench proved the edict to be bad in law, because it would be a violation of abstract justice, an impairment of vested rights, and a breach of the ancient constitution of France:

"The Parliament has not registered the edict for the suppression of the corveé, because this suppression would be against justice."

"The first rule of justice is to preserve to every one what belongs to him: this rule consists, not only in preserving the rights of property, but still more in preserving those belonging to the person, which arise from the prerogative of birth and of position. . . . From this rule of law and equity it follows that every system which, under an appearance of humanity and beneficence, would tend to establish between men an equality of duties, and to destroy necessary distinctions, would soon lead to disorder (the inevitable result of equality), and would bring about the overturn of civil society." Life and Writings of Turgot, Stephens, p. 132.

Reasoning from these premises Parliament concluded that the King might tax the peasantry at pleasure, or force them to labor gratuitously on the ways; of this the peasants could not complain, for they had no natural franchises, but that the nobility and the clergy enjoyed natural franchises which even the King could not abridge. After listening to this exposition of the law Louis XVI wrote these words to Turgot which were remembered long: "I see that you and I alone really love the people."

Nevertheless, Turgot was not to be turned from his purpose. He insisted that Parliament should be overruled. His advice prevailed, but at the cost of his political life. On

March 12, 1776, Louis XVI exerted the whole power of the Crown, and peremptorily ordered Parliament to register the edicts. Accordingly the edicts were registered, but instantly a resistless coalition of all the privileged classes of France assailed Turgot. This coalition extorted Turgot's dismissal from the King on May 12, 1776, just two months after his edict became law. With Turgot's fall the Revolution became inevitable; yet, with the chasm yawning before them, those who had so well defended their "natural franchises," felicitated themselves on the disgrace of the only man who could have saved them. Turgot's biographer has described the exultation with which the news was received at Versailles:

"When they knew at Versailles that M. Turgot had received his dismission, the joy was indecent, the laughter loud and long, and the felicitations mutual in the gallery, in the ante-chamber, and in the chamber of the King, and the same scene was repeated in Paris amongst those who lived upon abuses. This is as high a panegyric as any panegyric could be, it is among those which history should not neglect to record." Œuvres de Turgot, Paris, 1811, vol. I, p. 410.

Every spoliation of the weak, every violation of what we Americans have been taught to call our common right, has been vindicated by the same argument, whether that argument has been advanced by the Chief Justice of England, in the case of Sir Edward Hales, by the Parliament of Paris in opposition to Turgot, or by the defendants and interveners in this cause. Those who have been privileged, have ever asserted their privilege to be a natural franchise, enjoyed by them as a gift from Providence, which it would be folly or impiety to impair. Nor have the possessors of these franchises hesitated to put their principles to the proof, and the catastrophes which have followed may well be pondered in view of the coalition of the interveners with the defendants to cause this country to pass under servitude to monopoly.

Charles I, having repudiated the trust imposed on him by Magna Charta, in defence of his divine right to tax arbitrarily, met those who believed men to be equal before the law, at Naseby and at Dunbar; afterwards he atoned for his acts upon the scaffold before Whitehall.

The Parliament of Great Britain, pretending to be absolute, took money from the American colonies for the selfish use of England, and not for the welfare of all. Thereupon the colonists sundered the British empire.

The whole generation of French priests and nobles who cast out Turgot for counseling that their natural franchises should be abrogated, perished in the Terror of Robespierre.

Before 1861 the aristocracy which ruled the South refused all compromise with the North because, as the Chief Justice of the United States explained, God had intended the black man to be a slave. "They had for more than a century before been regarded as beings of an inferior order, and altogether unfit to associate with the white race; " therefore the white man believed "that the negro might justly and lawfully be reduced to slavery for his benefit." Dred Scott *v.* Sandford, 19 How., 407.

Your Honors know how our people answered this decision, and the fate which befell the South.

BROOKS ADAMS,
of Counsel for Complainants.

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(The financial returns to stockholders other than dividends are indexed as "Benefits.")